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UNITED STATES TAX COURT

REPORTS

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March 1, 2022, to
June 30, 2022

UNITED STATES TAX COURT

WASHINGTON, D.C.

JUDGES OF THE UNITED STATES TAX COURT

Chief Judge

MAURICE B. FOLEY

Judges

JOSEPH H. GALE
DAVID GUSTAFSON
ELIZABETH CREWSON PARIS
RICHARD T. MORRISON
KATHLEEN KERRIGAN[1]
RONALD L. BUCH
JOSEPH W. NEGA
CARY DOUGLAS PUGH
TAMARA W. ASHFORD
PATRICK J. URDA
ELIZABETH A. COPELAND
COURTNEY D. JONES
EMIN TORO
TRAVIS A. GREAVES
ALINA I. MARSHALL
CHRISTIAN N. WEILER

Senior Judges recalled to perform judicial duties under the provisions of section 7447 of the Internal Revenue Code:

MARY ANN COHEN
THOMAS B. WELLS
JOHN O. COLVIN
JAMES S. HALPERN
JUAN F. VASQUEZ
MICHAEL B. THORNTON
L. PAIGE MARVEL
JOSEPH ROBERT GOEKE
MARK V. HOLMES
ALBERT G. LAUBER

Special Trial Judges

LEWIS R. CARLUZZO, *Chief Special Trial Judge*

PETER J. PANUTHOS
DANIEL A. GUY, JR.[2]
DIANA L. LEYDEN
ADAM B. LANDY
EUNKYONG CHOI

STEPHANIE A. SERVOSS, *Clerk*

SHEILA A. MURPHY, *Reporter of Decisions*

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[1] Judge Kerrigan succeeded Judge Foley as Chief Judge on June 1, 2022.
[2] Special Trial Judge Guy retired March 29, 2022.

IN MEMORIAM

THE HONORABLE ROBERT P. RUWE

Judge, United States Tax Court

THE HONORABLE JOEL GERBER

Judge, United States Tax Court

IN MEMORIAM

Retired Tax Court Judge Robert P. Ruwe passed away on February 12, 2022. Judge Ruwe was known for his extraordinary memory and grasp of tax law and for the valuable experience he brought to his work.

Robert P. Ruwe was born in Ohio and graduated from Roger Bacon High School in St. Bernard. He attended Xavier University in Cincinnati on a football scholarship and graduated in 1963 with a B.A. and on the Dean's List. He worked as a special agent for the Intelligence Division of the IRS and went to law school at night, graduating first in his class from Salmon P. Chase College of Law in 1970. He served in the Ohio National Guard at the same time. Judge Ruwe joined the Office of Chief Counsel and rose through the ranks until he was Assistant Chief Counsel, Tax Litigation.

In 1987, President Ronald Reagan appointed him to the Tax Court. After his term ended, he served as a senior judge until his retirement in November 2020. On April 27, 2012, he received the J. Edgar Murdock Award for distinguished service to the Court. His contributions on and off the Court will be missed.

Judge Ruwe is survived by his wife, Mary Kay; 4 sons; 12 grandchildren; 2 brothers; and a legacy of mentorship, collegiality, and cogent jurisprudence.

Tax Court Judge Joel Gerber passed away on March 4, 2022. Judge Gerber received his B.S. in Business Administration from Roosevelt University, his J.D. from DePaul University Law School, and his LL.M. in Taxation from Boston University Law School. Prior to his appointment to the Court, Judge Gerber spent many years working for the Internal Revenue Service: as a trial attorney in Boston, Massachusetts; as a senior trial attorney in Atlanta, Georgia; as District Counsel in Nashville, Tennessee; and as Deputy Chief Counsel in

Washington, D.C. He was also Acting Chief Counsel from May 1983 to March 1984.

Judge Gerber was appointed for his first term by President Reagan in 1984, and for his second term by President Clinton in 2000. Judge Gerber was Chief Judge of the Court from June 1, 2004, until May 31, 2006. He served as a senior judge on recall from June 1, 2006, until July 16, 2020.

Judge Gerber had a zest for life and was a humble, humorous, and unabashedly compassionate man who endeared himself to colleagues, employees, and all those fortunate enough to cross his path. His contributions on and off the Court will be missed.

Chicago, Illinois

March 14, 2022

HONORABLE PATRICK J. URDA

THE COURT: Thank you all for being here, and it's nice to be back in Chicago.

Before we proceed to trial, I would like to acknowledge the passing of two pillars of the Tax Court, Judge Robert Ruwe on February 12 and Judge Joel Gerber on March 4.

Joel Gerber, as I'll talk about him in just a minute, was a graduate of DePaul, here in Chicago, but let's start with Judge Ruwe.

Judge Ruwe was born in Ohio and graduated from Roger Bacon High School, an outstanding all-boys school with a championship football team on which he played all four years. He attended Xavier University in Cincinnati on a football scholarship and graduated with a B.A. from that school.

He worked as a special agent for the Intelligence Division of the IRS and went to law school at night, graduating first in his class at Salmon P. Chase College of Law in 1970. While working for the IRS and studying at night, he also found time to serve his state and this nation in the Ohio National Guard.

Judge Ruwe joined the Office of Chief Counsel and rose through the ranks until he was Director of the Tax Litigation Division. In 1987, he was appointed by President Reagan to the Court. After his term ended, he served as a senior judge until his retirement in November 2020. He also received the Tax Court's highest honor, the J. Edgar Murdock Award for distinguished service on April 27, 2012. Judge Ruwe was a great mentor to generations of clerks, and I can speak from experience that he graciously extended this mentorship to new judges as well. He gave me the chance to benefit from his deep insights into tax law as well as from many personal courtesies.

Judge Ruwe is survived by his wife of more than 55 years, 4 sons, 12 grandchildren, 2 brothers, and a legacy of adoring clerks and cherished colleagues.

Turning to Judge Gerber. Judge Joel Gerber received his B.S. in business administration from Roosevelt University and his J.D. here at DePaul. He also received an LL.M. in taxation from Boston University School of Law. Prior to his appointment to the Court, Judge Gerber served with the IRS in Boston, Atlanta National, and D.C. He was the Acting IRS Chief Counsel from May 1983 to March 1984.

Judge Gerber was appointed for his first term by President Reagan in 1984, and for his second term by President Clinton in 2000. Judge Gerber served as a senior judge on recall from June 1, 2006, until July 16, 2020. He was Chief Judge of the Court during a particular time of transition from June 1, 2004, until May 31, 2006, where we were dealing with the complicated aftermath of cases such as *Kanter v. Commissioner* and *Ballard v. Commissioner*.

Judge Gerber was a raconteur par excellence. He was legendary at the Court for his humility, humor and compassion, not just for Court personnel, but really, anyone who came across his path. He had a true zest for life and a desire to help others. He was devoted to his wife of almost 60 years, as well as his three sons and seven grandchildren.

Needless to say, the Tax Court will miss Judges Ruwe and Gerber. We'll miss them both for their brilliance as jurists, but more importantly, for who they were as people.

Columbia, South Carolina

March 21, 2022

HONORABLE DAVID GUSTAFSON

THE COURT: Please be seated.

THE CLERK: All persons having business before the United States Tax Court will please give their attention. The Court is now in session. Judge Gustafson is presiding.

THE COURT: Before we begin the trial for which we meet this week, I would like to follow the Tax Court's custom of acknowledging at sessions of the Court the recent death of one of its judges, in this instance, Judge Robert P. Ruwe, who died February 12, 2022.

Judge Ruwe was appointed to the Court by President Ronald Reagan and served for 33 years. Other Tax Court judges at other sessions will describe his prodigious accomplishments, so I would like to restrict myself to a personal reminiscence.

My first acquaintance with Judge Ruwe was about 35 years ago, when I was an attorney with the Tax Division of the U.S. Department of Justice and Robert Ruwe was the director of the IRS Tax Litigation Division. In a suit I handled in the U.S. Court of Federal Claims, I wanted to raise a new issue that had not been recommended by the Chief Counsel of the IRS, and our procedures required me to get the IRS's concurrence in raising that issue. It was Robert Ruwe who had to decide.

Unconvinced by my arguments, he declined to approve the raising of the issue. He concluded that there was not suffcient evidence to warrant making that argument against the taxpayer.

At the time I disagreed and was disappointed, but the reason I bring it up today is that it revealed, even before he was a judge, that Robert Ruwe had a judicial temperament. He was impartial, dispassionate, attentive, and discerning. He wanted simply to make the correct decision, to do the right thing, without regard to partisan interests.

Years later, in 2008, when I became his colleague—I will not say peer—I saw the same stellar character in my closeup observation of his work as a judge. He was a kind, friendly, generous, helpful, and wise mentor. I owe him a great deal, and I will miss him.

Atlanta, Georgia

March 21, 2022

HONORABLE KATHLEEN KERRIGAN

THE COURT: And during the course of the last two months, two judges from the Tax Court passed away. Judge Joel Gerber passed away on March 4, 2022. And Judge Robert Ruwe passed away on February 12, 2022. When I came to the Court, they were both senior judges. And they both were mentors of mine.

Judge Ruwe, I thought, wrote really good opinions. So he sat down with me and my clerks at the very beginning to talk about how he approached writing an opinion. And I always thought that was very helpful advice. And the Court has a dining room where the judges eat, and Judge Ruwe was there most days. So whenever there was something on my calendar, or I wasn't sure what to do with something, I'd run down to the lunchroom at lunchtime, knowing I would get a very wise answer.

Judge Gerber, I met—I'd only been at the Court couple of weeks. I was supposed to go out to Los Angeles to observe another judge do a trial. I'm in the cab on the way to the airport, and I checked my email, the judge that I was supposed to do the trial session was hospitalized and would no longer be able to do the session. And I thought, well, they'd better be having someone else. I don't know how to do this.

So Judge Gerber, who was a senior judge, lived in San Diego, in the San Diego area, took the train to L.A. And I met him in L.A. And we proceeded with the calendar session the next day. And it was a lengthy calendar, but it wound up only having two trials. And he said, I'll do the first one, and you'll do the second. I'm almost done with the second trial and I see the marshal come in and say something to Judge Gerber. And I'm, kind of, like, uh-oh, what is going on? And then, Judge Gerber passed me a note. And I had to read, "Please, we all—please leave the building quietly and quickly. There's a bomb scare." So I said, that gives trial by fire a new meaning. So that is how I started at the Court.

And during the years, I appreciated the friendship of Judge Ruwe and his wife, Mary Kay, and Judge Gerber and his wife, Judi. And I just wanted to take a few minutes to remember these two because they were wonderful judges and had a great influence on the Court.

And so we will now be in recess for half an hour, which will bring this to 20 of 11. Thank you.

Spokane, Washington

March 21, 2022

HONORABLE JOSEPH W. NEGA

THE COURT: Good morning to everybody in California. I would like to acknowledge the recent passing of Judge Joel Gerber and Judge Robert Ruwe. Judge Gerber received his B.S. in business administration from Roosevelt University, his J.D. from DePaul University Law School, and his LL.M. in taxation from Boston University Law School.

After growing up on the North Side and attending undergrad and law school in Downtown Chicago, Judge Gerber found his way to the Internal Revenue Service, assuming ever more responsible positions at the IRS and serving in Boston, Atlanta, Nashville, and Washington, D.C. He achieved the pinnacle of an IRS attorney. He served as Acting IRS Chief Counsel from May 1983 to March 1984.

Judge Gerber was selected for what he called his dream job as judge on the United States Tax Court by President Ronald Reagan and was appointed for a second term by President William Clinton. Judge Gerber was elected by his fellow judges to the position of Chief Judge in 2006.

During his tenure as Chief Judge, the Tax Court made the transition to computers and email. He was also tasked with shaping the Tax Court's response to two significant legal decisions: *Kanter v. Commissioner* and *Ballard v. Commissioner*. His efforts resulted in an even stronger Tax Court. After his two-year term as Chief Judge, Judge Gerber served as a senior judge on recall for 14 years before retiring to sunny California.

Judge Robert Ruwe also grew up in the Midwest. He was born in Ohio. He played all four years on his high school football team. That team won a championship. He received a football scholarship to Xavier University and played on its football team. After graduating from college on the dean's list, Judge Ruwe found work as a special agent for the Intelligence Division of the IRS.

While working full time at the IRS and serving in the Ohio National Guard, he attended law school at night. Judge Ruwe graduated first in his class from the Salmon P. Chase College of Law. Judge Ruwe joined the Office of Chief Counsel, and like Judge Gerber, assumed ever more responsible jobs until he was made Director of the Tax Litigation Division.

In 1987 Judge Ruwe was also nominated to the Tax Court by President Ronald Reagan. At the end of his 15-year term, Judge Ruwe continued to serve as a senior judge on recall until November 2020. If you are not impressed yet, then you have not been listening. However, these two wonderful men were so much more than their careers. Let me mention a few more personal notes.

I first met then Chief Judge Gerber at an alumni dinner for Washington D.C.-based alumni of DePaul University School of Law. When he heard that I was a government tax attorney, he spent a long time discussing Chicago and my then job on Capitol Hill. At the next such dinner, Judge Gerber not only remembered me, but asked for an update on my life.

Like Judge Patrick Urda and myself, Judge Gerber always had a soft spot for the Chicago Cubs. He was also an avid cyclist. I mention this because after I joined the Tax Court, I met him in the men's locker room at the Court after our workouts. He asked how I was fitting in and whether or not there was any advice he could offer. When I complained that my exercise routine had been disrupted by my new work hours, he immediately offered a suggestion.

It was simple; start commuting every day by bicycle. When I protested that it was nearly ten miles, he replied that was about the length of his daily bicycle commute when he lived in Virginia. Sometime later, Judge Gerber followed up to see whether or not I had tried his advice.

I met Judge Ruwe for the first time in the Tax Court cafeteria after my swearing in. He was just as willing to share his advice about my new job. All I had to do was ask; I made a point to ask.

These two men certainly had many other professional options. However, in an environment when all too frequently government employees are derided as lazy, inept, or worse, these two fine men devoted their professional lives to making government work better. They will be greatly missed.

Judge Gerber is survived by Judi, his wife of nearly 60 years; three children; and several grandchildren. Judge Ruwe is survived by Mary Kay, his wife of 55 years; 4 sons; and 12 grandchildren. These were truly two men with lives well lived.

Thank you for your attention. And I'll have Mr. Mason call out the docket for Spokane.

Indianapolis, Indiana

March 21, 2022

Honorable Elizabeth A. Copeland

The Clerk: All rise. All persons having business before the United States Tax Court will draw near and give their attention. The Court is now in session. Judge Copeland is presiding.

The Court: You may be seated. Good morning. I am Judge Copeland. And welcome to the March 21 session of the United States Tax Court. Before we begin with the regular announcements for this trial session, it's both my sad duty and my privilege to pay tribute to two judicial legends who very recently passed away, Judge Robert P. Ruwe and Judge Joel Gerber.

I will begin with the life and career of Judge Robert P. Ruwe. Judge Ruwe served on the Tax Court from 1987 through 2020, a total of 33 years. He was appointed to the Court by President Ronald Reagan. Judge Ruwe's career was illustrious by any standard. Before becoming a judge on the Tax Court, he was a special agent in the Internal Revenue Service Intelligence Division for seven years. He then joined the IRS Office of Chief Counsel as a trial attorney, and climbed up the ranks to become Director of the IRS Tax Litigation Division. During his tenure with the Tax Court, he authored 141 division opinions, 399 memorandum opinions, and 92 summary opinions.

He was known for his extraordinary memory and excellent grasp of the tax law. Judge Ruwe received the J. Edgar Murdock Award for distinguished service to the Court on April 27, 2012. One of my very first cases that I tried as a young attorney was before Judge Ruwe. I found him to be fair, thoughtful, and an effective jurist. Judge Ruwe died on February 12, 2022. He's survived by his wife, Mary Kay; 4 sons; and 12 grandchildren. And he shall be missed.

Next, I would like to honor Judge Joel Gerber, who served on the Tax Court from 1984 through 2020, a total of 36 years. He was appointed to the Court by President Ronald Reagan in 1984 and for his second term by President Bill Clinton in 2000. Judge Gerber served as a senior judge on recall from June 1, 2006, until July 16, 2020. He was Chief Judge of the Court from June 1, 2004, until May 31, 2006.

Prior to his appointment to the Court, Judge Gerber worked as a trial attorney in the Internal Revenue Service Office of Chief Counsel in Boston and Atlanta. He was District Counsel in Nashville and Deputy Chief Counsel in Washington D.C. He was the Acting IRS Chief Counsel from May 1983 to March 1984.

Being a Tax Court judge was a natural fit. His intelligence and temperament he had for the job. He was an excellent jurist. During his tenure at the Court, he authored 127 division opinions, 558 memorandum opinions, and 115 summary opinions. His time with the Court was not without challenges, however. During his tenure as Chief Judge, he transitioned the Court electronically to the use of computers and email. He likewise deftly dealt with the complicated aftermath of the *Kanter* and *Ballard* cases. *Kanter*'s cite is 406 F.3d 933 (7th Cir. 2005). And *Ballard*'s is 125 S. Ct. 1270 (2005). Both were cases in which the Court was under extreme scrutiny. He openly addressed the issues and took steps to ensure transparency in the decision-making process at the Court.

Judge Gerber was humble, humorous, and unabashedly compassionate. He was a humanitarian, a cyclist, an avid traveler, a gourmet cook, and a woodworker, among other things. I fondly remember cycling beside Judge Gerber to the Tax Court when I was a law clerk for the Court. He's survived by his wife, Judi, of almost 60 years; three sons; and seven grandchildren. He likewise will be missed.

Thank you. We are going to briefly go off the record for a moment of silence for these two men.

St. Paul, Minnesota

March 21, 2022

HONORABLE MARK V. HOLMES

THE CLERK: All persons having business for United States Tax Court shall join and give their attention. The Court is now in session. The Honorable Judge Holmes presiding.

THE COURT: To those who are here, it is the custom of the Tax Court to briefly eulogize judges when they die. In the last several weeks, we lost Judge Robert Ruwe and Judge Joel Gerber.

Judge Ruwe was already a senior judge when I started. But he was a constant presence at the Court all the way through 2020. He'd been appointed by President Reagan and served a total of 33 years. Judge Ruwe was notable at our Court for having once held the power to carry a gun and arrest people, not as a way of keeping his colleagues in line, but because his path to judging began as a special agent at the IRS in its Intelligence Division. Only after seven years in law enforcement did he become a trial lawyer at Chief Counsel and then rise as a trial attorney to eventually become Director of the IRS Tax Litigation Division.

He was a Santa Claus figure in his later years at the Court and was always notable for being a fair and effective judge. Judge Ruwe died on February 12. He is survived by his wife, Mary Kay; four sons; and a dozen grandchildren. He shall be missed.

Judge Gerber was also a Reagan appointee, and a Clinton reappointee. And he served for a total of 36 years. He was a very active regular judge when the group of five new judges, of which I was a part, arrived back in 2003. One of us five had clerked for him. All of us quickly became his friends and pupils.

We were so taken with him that we prevailed upon him to run for Chief Judge. He served in that job for only two years, but what a two years. When we arrived, the Court did not have voicemail. Our clerks had no internet access. And the Clerk's Office kept track of calendars by crossing cases off in three-ring binders. All this changed very quickly. Chief Judge Gerber got the building wired for internet access for everyone, moved our phones from the 1970s to a voice-over-internet protocol, and started the Court's long slog toward electronic records and filing. In showing his Reaganite roots, he did all this while asking Congress to lower our budget as we cut back on unnecessary spending.

But as much as his colleagues appreciated him as a leader, he was foremost a wonderful judge. One of my favorite Gerber stories is one he told me about his early years as a judge. He was taken aback the first time he sensed a witness was lying. As he told the story, he stopped the trial and went off the record. He reminded the witness that he was under oath. And then he got a little personal. He said that his mom was very proud when her son had become a judge, and had reminded him when he was sworn in that you should always treat people fairly and do his job with compassion as best he could. He told the witness that it would make his mother very sad if he had to tell her that, instead of just deciding his case, he had to make a referral of the witness for a perjury investigation. That isn't what his mother wanted him to do, he said. And he didn't want to do it, and maybe the witness should think twice and try again. They went back on the record. And the witness told the truth. And the case was decided on its merits.

Shortly afterward, the same thing happened to me. A witness was pretty clearly lying. I was impressed with Judge Gerber. I wanted to be as good a judge as Judge Gerber. So I went off the record. I looked down at the witness, and I said, "Stop lying or Ms. Gerber will be very sad." Not quite the same effect. But then, I'm no Judge Gerber.

Joel Gerber was smart and compassionate and funny and wise and a great teacher, a real mensch. Judge Gerber was a great man and a great Tax Court judge. He leaves behind his wife, Judi; their three sons; and seven grandchildren. May God comfort them among the mourners of Zion and Jerusalem.

We will now briefly go off the record for a moment of silence in honor of these two men.

San Francisco, California

March 21, 2022

Special Trial Judge Diana L. Leyden

The Court: Good morning, everyone. Thank you for joining us today. I was giving some opening remarks, but before we start, the Court has a tradition in sessions after a judge has passed to give a small tribute to the judge. And sadly, we lost two judges recently. And so I'd like to give you some opening remarks in tribute to those judges.

The first judge was Judge Robert Ruwe. And he had quite a long history with the Court and outside the Court. He was appointed by President Ronald Reagan, and he served on the Tax Court from 1987 to 2020, a total of 33 years. Even before that, he had quite an interesting career.

He started as a special agent with the Internal Revenue Service's Intelligence Division, in which he served for seven years. Then as an attorney, he served with the IRS Office of Chief Counsel as a trial attorney, and then later as a director of the IRS Tax Litigation Division.

He authored quite a number of opinions at the Tax Court. He authored 141 division opinions, 399 memorandum opinions, and 92 summary opinions. He had quite an extraordinary memory and an excellent grasp of tax law. Judge Ruwe also received the J. Edgar Murdock Award, which is given for someone in the Court for distinguished service to the Court. He received that on April 27, 2012.

I was a new special trial judge in 2016. And the first time I met Judge Ruwe, he was very welcoming and very kind to me, and I'll always remember that. He died on February 12, 2022, and he is survived by his wife, Mary Kay; 4 sons; and 12 grandchildren.

Sadly, we also lost another wonderful judge, Judge Joel Gerber. He served on the Tax Court from 1984 to 2022, also appointed by President Reagan. And he was reappointed for a second term by President Clinton in 2000. He was a senior judge from June 1, 2006, until July 16, 2020. And he also served in the role of Chief Judge of our Court from June 1, 2004, to May 31, 2006.

Prior to his appointment to the Court, he also served as an attorney in the Internal Revenue Service Office of Chief Counsel in Boston and Atlanta, was District Counsel in Nashville, Tennessee; Deputy Chief Counsel in Washington, D.C.; and was the Acting IRS Chief Counsel from May 1983 to March 1984.

He had just a wonderful temperament. He was very compassionate, he was very intelligent. He also was quite prolific in his opinions. During his tenure, he authored 127 division opinions, 558 memorandum opinions, and 115 summary opinions. He was very humble, very humorous, and as I said, quite compassionate. He was humanitarian, a cyclist, an avid traveler, a gourmet cook, and a woodworker.

If anyone is interested, if you go on our tax website, he had a bit of an incident woodworking while he was in his home in California. Something kicked back and hit him, and he actually passed out. And but for a postal worker coming by at the right time, he probably would have died prior to when he did die. And he had this wonderful tribute to the postal service worker; I think it was just very in character of Judge Gerber.

He is survived by his wife, Judi, of almost 60 years; three sons; and seven grandchildren. If you would for a minute, we'll go off record, but I would like everyone to pay some tribute to these wonderful jurists. If we could just have a moment of silence in honor of them. Thank you.

(Pause.)

THE COURT: Thank you very much.

Washington, DC

March 24, 2022

HONORABLE TAMARA W. ASHFORD

THE COURT: There are no other matters for the Court with this session, but before I adjourn this session of the Court, I would like to take this opportunity to pay tribute to and remark on the incredible life and career of two judicial giants of the Tax Court who recently passed away. I think, certainly, Mr. Probasco, Mr. Begun, and Mr. Livermore are probably aware, as well as Ms. Finken, recently my dear colleagues Judge Robert P. Ruwe and Judge Joel Gerber have departed us.

And so let me start with Judge Ruwe. It was February, just last month, that Judge Ruwe peacefully passed away at home surrounded by his loving family. He served on the Court for a total of 33 years, having been appointed to the Court in 1987 by President Reagan. And after his 15-year term ended in 2002, he served as a senior judge on recall to this Court until his retirement in November of 2020.

Judge Ruwe was a true public servant in every sense of the word. First, he actually worked as a special agent for the Intelligence Division of the IRS and went to law school at night, graduating first in his class from Salmon P. Chase school of law in 1970. He also served in the Ohio National Guard at the same time. Upon graduating from law school, Judge Ruwe joined the IRS Office of Chief Counsel as a trial attorney and rose through the ranks to become the Assistant Chief Counsel of the Tax Litigation Division.

Judge Ruwe was known for his extraordinary memory and grasp of tax law. During the 33 years that he served on the Court, he wrote 533 opinions, 141 division or T.C. opinions, 399 memorandum opinions, and 92 summary opinions. And in recognition of his outstanding service to the Court, on April 27, 2012, he received the J. Edgar Murdock Award for distinguished service.

Outside of the Court, Judge Ruwe loved spending time with his family and friends, reading about the Civil War, and eating chocolate chip ice cream, which is one of my favorites, from Cincinnati, Ohio, his home-state-based ice creamery, Graeter's.

Judge Ruwe is survived by his wife of more than 55 years, Mary Kay; 4 sons; 12 grandchildren; and a legacy of adoring clerks and cherished colleagues.

Judge Gerber. Earlier this month, Judge Gerber passed away after a brief illness. Judge Gerber's career was similarly illustrious by any standard. Before being appointed to the Tax Court, Judge Gerber served as a trial attorney with the IRS Chief Counsel in Boston, as a senior trial attorney with IRS Chief Counsel in Atlanta, as IRS District Counsel in Nashville, and as Deputy Chief Counsel in Washington, D.C. He was the Acting Chief Counsel from May 1983 to March 1984.

Being a Tax Court judge was his dream job. He was first appointed to the Court by President Reagan in 1984 and was reappointed to the Court by President Clinton in 2000. From June 2004 to May 2006, he was the Chief Judge of this Court. Thereafter, he served as senior judge on recall until his retirement in July 2020.

During the 36 years that he served on the Court, Judge Gerber wrote 800 opinions: 127 Division opinions, 558 memorandum opinions, and 115 summary opinions. I should also mention that during his time as Chief Judge, it was a time of significant transition for the Court, transition to computers and email, if you can believe that, and the complicated aftermath of the *Kanter v. Commissioner* and *Ballard v. Commissioner* cases. Judge Gerber deftly handled the technology and the *Kanter*, *Ballard* issue. And more specifically as to the latter issue, he openly addressed the issue and took steps to ensure transparency in the decision-making process of the Court.

Judge Gerber was a humble, humorous, and unabashedly compassionate man who loved his family and his friends. Indeed, on many occasions, he would come to my chambers and, in addition to imparting great court wisdom, would share stories about his travels, cooking, woodworking, and bicycling. What a raconteur he was.

Judge Gerber is survived by his wife, Judi, of almost 60 years; three sons; seven grandchildren; and also a legacy of adoring clerks and cherished colleagues.

I feel so fortunate to have crossed paths with both of these fine jurists. They shall be sorely missed. Rest in peace, Judges Ruwe and Gerber. And continued blessings to his family and close friends.

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GINA C. LEWIS, PETITIONER *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 12930-18. Filed March 3, 2022.

P and her former spouse filed joint federal income tax returns for 2008, 2009, and 2010. The IRS audited and proposed adjustments to those returns. In December 2016, P submitted a letter to the IRS that purported to be a qualified offer under I.R.C. § 7430(g). In it, P offered to concede 100% of the tax and penalties set forth in the IRS's proposed adjustment but reserved the right to claim relief from joint and several liability under I.R.C. § 6015. The IRS did not accept P's offer and later issued a notice of deficiency. In her petition P claimed relief from liability under I.R.C. § 6015. In his answer R indicated that he would consider P's entitlement to relief from liability under I.R.C. § 6015 once P provided R with relevant documentation, such as Form 8857, Request for Innocent Spouse Relief. P did not provide Form 8857 to R's counsel or to the IRS's Cincinnati Centralized Innocent Spouse Operation. After reaching a settlement with Intervenor, R conceded that P is entitled to relief from liability under I.R.C. § 6015(c) for the years in issue. Concurrently, R moved for entry of decision reflecting no liabilities for the years in issue after the application of I.R.C. § 6015(c). P objected to R's motion for entry of decision on the ground that it was an attempt to prevent P's claim for litigation costs. P then moved for litigation costs under I.R.C. § 7430.

1. *Held*: I.R.C. § 6015 provides relief from joint and several liability, not just collection.

2. *Held, further*, a qualified offer must "specif[y] the offered amount of the taxpayer's liability," I.R.C. § 7430(g)(1)(B), and must be "an amount, the acceptance of which by the United States will fully resolve the taxpayer's liability, and only that liability . . . for the type or types of tax and the taxable year or years at issue in the proceeding," Treas. Reg. § 301.7430-7(c)(3).

3. *Held, further*, an offer that reserves the right to claim relief from liability for income tax under I.R.C. § 6015 is not a qualified offer because it does not specify the offered amount that, if accepted, would fully resolve the taxpayer's income tax liability under I.R.C. § 7430(g)(1)(B) and Treas. Reg. § 301.7430-7(c)(3).

4. *Held, further*, P's offer was not a qualified offer under I.R.C. § 7430(g)(1)(B) and Treas. Reg. § 301.7430-7(c)(3).

5. *Held, further*, P is not entitled to litigation costs under I.R.C. § 7430 because respondent's position was substantially justified.

Steve Milgrom, for petitioner.
Vincent A. Gonzalez and *Emma S. Warner*, for respondent.

OPINION

PUGH, *Judge*: This case is before the Court on petitioner's motion for reasonable litigation costs (motion for litigation costs) pursuant to section 7430 and Rule 231.[1] We conclude that petitioner is not a "prevailing party" within the meaning of section 7430. We therefore will deny her request for litigation costs.

Background

The following facts are derived from the parties' pleadings and motion papers. These facts are stated solely for the purpose of ruling on petitioner's motion and not as findings of fact in this case. Petitioner resided in California when she filed her petition.

Petitioner and her former spouse, Tim S. Lewis, filed joint federal income tax returns for 2008, 2009, and 2010. The Internal Revenue Service (IRS) audited these returns and proposed adjustments and penalties for petitioner and Mr. Lewis.

On December 28, 2016, petitioner sent to the IRS a letter (December 2016 offer letter or offer) stating that she was making a qualified offer pursuant to section 7430(g). She offered the following terms:

> 1. To concede 100% of the tax and 100% of the penalties for the tax years 2008, 2009, and 2010, as set forth on the attached Form 4549-A dated February 12, 2013.
> 2. To agree to the immediate assessment of the increase in tax and penalties set forth on the attached Form 4549-A.
> 3. This is an offer of assessment, not payment, Mrs. Lewis reserves all collection rights that she may qualify for now or in the future, including without limitation, the right to relief under IRC §6015 (innocent spouse), §6159 (installment agreement), §7122 (offer in compromise), §6343 (release of levy), §7811 (taxpayer assistance order), §6502 (statute of limitations on collection), §6325 (release of lien), collection due process, collection appeals program, currently non-collectible status, bankruptcy, and

[1] Unless otherwise indicated, all statutory references are to the Internal Revenue Code, Title 26 U.S.C., in effect at all relevant times, all regulation references are to the Code of Federal Regulations, Title 26 (Treas. Reg.), in effect at all relevant times, and all Rule references are to the Tax Court Rules of Practice and Procedure.

any other current or future law that may serve to reduce the amount or delay the payment of amounts assessed as a result of the acceptance of this qualified offer.

The IRS neither accepted nor rejected the qualified offer, and instead allowed it to lapse.

In the months before petitioner submitted her offer, the revenue agent's activity record reflects discussion of petitioner's entitlement to innocent spouse relief under section 6015. Petitioner did not provide any information to support a claim for innocent spouse relief or submit a Form 8857, Request for Innocent Spouse Relief, prior to or contemporaneously with the December 2016 offer letter.

On March 28, 2018, respondent issued a notice of deficiency to petitioner and Mr. Lewis, determining deficiencies and penalties for tax years 2008, 2009, and 2010.

On July 2, 2018, petitioner timely filed her petition, and in her timely amended petition she "elect[ed] the benefits" of section 6015(b) and (c). In his answer to her amended petition, respondent: "Admit[ed] [p]etitioner has requested innocent spouse relief in her petition per I.R.C. § 6015(b)&(c) and [r]espondent will review her request and make a determination regarding her eligibility for said relief." Mr. Lewis also challenged the notice of deficiency at docket No. 12785-18 and intervened in petitioner's case pursuant to Rule 325.

Throughout the proceeding, respondent requested that petitioner submit Form 8857 or provide other information supporting her claim for innocent spouse relief under section 6015. Petitioner never did. Nonetheless, respondent's counsel referred the case to the IRS Cincinnati Centralized Innocent Spouse Operation (CCISO), which requested the Form 8857 and supporting documentation from petitioner. She did not submit Form 8857 and supporting documentation to CCISO either. Eventually, after resolving the related case with Mr. Lewis, respondent concluded that petitioner was entitled to innocent spouse relief under section 6015(c).[2]

On December 28, 2020, respondent moved for entry of a decision that would grant petitioner full relief from joint and several liability under section 6015(c) for tax years 2008, 2009, and 2010; after application of section 6015(c), the

[2] After stipulating to entry of decision in docket No. 12785-18, Mr. Lewis moved to withdraw as intervenor in this case and we granted his motion.

deficiency and the penalty for each year are listed as "None." He also filed a notice of concession "that [p]etitioner is entitled to relief under section 6015(c) for tax years 2008, 2009, and 2010." Petitioner objected to the motion for entry of decision and the notice of concession, claiming that it was a "litigation tactic to avoid an award of fees and costs that [p]etitioner is entitled to."[3]

Petitioner eventually filed her motion for litigation costs after being ordered to do so by the Court. Respondent filed a response opposing petitioner's motion, and petitioner filed a reply.

Discussion

As relevant here, section 7430 provides for an award of reasonable litigation costs to a taxpayer in a proceeding brought by or against the United States involving the determination of any tax, interest, or penalty.[4] An award may be made where the taxpayer can demonstrate that she (1) is the "prevailing party," (2) has exhausted available administrative remedies within the IRS,[5] (3) has not unreasonably protracted the proceeding, and (4) has claimed "reasonable" costs. § 7430(a), (b)(1), (3), (c)(1); *Morrison v. Commissioner*, 565 F.3d 658, 661 (9th Cir. 2009), *rev'g on other grounds* T.C. Memo. 2006-103; *Alterman Tr. v. Commissioner*, 146 T.C. 226, 227 (2016). The taxpayer bears the burden of proving that these requirements are met. Rule 232(e). These requirements are conjunctive; failure to satisfy any one of them precludes an award of costs to the taxpayer. *See Alterman Tr.*, 146 T.C. at 227; *see also Minahan v. Commissioner*, 88 T.C. 492, 497 (1987). The decision to award fees is within the sound discretion of the Court. *See Morrison v. Commissioner*, 565 F.3d at 661 n.3 ("A decision by the Tax Court denying an award of attorneys' fees is reviewed for abuse of discretion." (citing *Huffman v.*

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[3] Petitioner refused to sign a stipulation of settled issues or decision document that stated that she is entitled to full relief from joint and several liability under section 6015(c) for 2008, 2009, and 2010, for similar reasons. At an impasse, respondent unilaterally filed his motion for entry of decision and notice of concession.

[4] Section 7430 also provides for an award of reasonable administrative costs incurred in connection with an administrative proceeding within the IRS. Petitioner has not requested such an award.

[5] This requirement applies only as to litigation costs. *See* § 7430(b)(1).

Commissioner, 978 F.2d 1139, 1143 (9th Cir. 1992), *aff'g in part, rev'g in part and remanding* T.C. Memo. 1991-144)).

Respondent disputes that petitioner satisfies each of the four requirements outlined above. We begin with the first requirement—that petitioner demonstrate that she is the prevailing party—and, in the light of our resolution of that issue, we need not address the other three.

I. *Prevailing Party*

To be the "prevailing party," a taxpayer must satisfy certain networth requirements, *see* § 7430(c)(4)(A)(ii), and must "substantially prevail[]" with respect to the amount in controversy or "the most significant issue or set of issues presented," *see* § 7430(c)(4)(A)(i). Respondent agrees that petitioner meets the net-worth requirements and substantially prevailed with respect to the amount in controversy and the most significant issue presented.

The taxpayer generally will not be treated as the prevailing party if the Commissioner establishes that "the position of the United States in the proceeding was substantially justified." § 7430(c)(4)(B)(i). The Commissioner bears the burden of making that showing. *Id.*; *see also* Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 701(b), 110 Stat. 1452, 1463 (1996) (adding current section 7430(c)(4)(B) to shift the burden of proving substantial justification from the taxpayer to the Government); *Pac. Fisheries Inc. v. United States*, 484 F.3d 1103, 1107 (9th Cir. 2007).

Even if the Commissioner's position is substantially justified, under section 7430(c)(4)(E)(i) the taxpayer shall be treated as the prevailing party if "the liability of the taxpayer pursuant to the judgment in the proceeding (determined without regard to interest) is equal to or less than the liability of the taxpayer which would have been so determined if the United States had accepted a qualified offer of the party under subsection (g)." *See Haas & Assocs. Acct. Corp. v. Commissioner*, 117 T.C. 48, 59 (2001) (holding that the qualified offer provision of section 7430(c)(4)(E)(i) applies without regard to whether the Commissioner's position in the matter is substantially justified), *supplementing* T.C. Memo. 2000-183, *aff'd*, 55 F. App'x 476 (9th Cir. 2003). The qualified offer provision may not apply, however, where the "judgment [is] issued pursuant to a settlement."[6] § 7430(c)(4)(E)(ii)(I). Petitioner bears the burden of proving that she meets the qualified offer requirements. *See* Rule 232(e).

We first consider whether petitioner is the prevailing party under the qualified offer provision, and, after concluding that she is not, turn to whether respondent's position was substantially justified.

II. *Qualified Offer Requirements*

A qualified offer is defined in section 7430(g)(1) as a written offer which:

> (A) is made by the taxpayer to the United States during the qualified offer period;
> (B) specifies the offered amount of the taxpayer's liability (determined without regard to interest);
> (C) is designated at the time it is made as a qualified offer for purposes of this section; and
> (D) remains open during the period beginning on the date it is made and ending on the earliest of the date the offer is rejected, the date the trial begins, or the 90th day after the date the offer is made.

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[6] As we noted above, petitioner rejected respondent's proposed settlement and concession to avoid a conclusion that judgment in this case will be "issued pursuant to a settlement" under section 7430(c)(4)(E)(ii)(I). *See Trzeciak v. Commissioner*, T.C. Memo. 2012-83 (holding that the Commissioner's concession was a settlement and distinguishing *Estate of Lippitz v. Commissioner*, T.C. Memo. 2007-293, 2007 WL 2780496, in which the Court held that the Commissioner's concession was not a settlement because the taxpayer was forced to actively litigate the case prior to the concession).

This Court and the U.S. Court of Appeals for the Ninth Circuit, to which an appeal would lie absent stipulation to the contrary, *see* § 7482(b), have held that a concession is not a settlement when the Commissioner waited to concede until after the taxpayer "had effectively presented the case for disposition by the Court," *Knudsen v. Commissioner*, 793 F.3d 1030, 1035 (9th Cir. 2015) (quoting *Estate of Lippitz v. Commissioner*, 2007 WL 2780496, at *8)), *rev'g and remanding* T.C. Memo. 2013-87. In *Knudsen* and *Estate of Lippitz*, that effective presentation included filing Form 8857 and providing additional documentation to the IRS. Here, petitioner refused to provide such documentation. But respondent does not argue that petitioner did not make a qualified offer because respondent's unilateral concession constituted a settlement. We therefore assume arguendo that the case will not be decided pursuant to settlement.

Treasury Regulation § 301.7430-7(c)(3) provides further guidance on the requirement that the offer "specif[y] the offered amount of the taxpayer's liability":

> [(1)] The offer may be a specific dollar amount of the total liability or a percentage of the adjustments at issue in the proceeding at the time the offer is made. [(2)] This amount must be with respect to all of the adjustments at issue in the administrative or court proceeding at the time the offer is made and only those adjustments. [(3)] The specified amount must be an amount, the acceptance of which by the United States will fully resolve the taxpayer's liability, and only that liability . . . for the type or types of tax and the taxable year or years at issue in the proceeding.

Respondent argues that petitioner's offer was not a qualified offer because it did not specify an amount "the acceptance of which by the United States will fully resolve the taxpayer's liability."[7] *Id.* Respondent emphasizes that petitioner's offer "merely conced[ed] the assessment of a tax but reserve[d] the right to later challenge that assessed liability by raising section 6015 relief."

In reply petitioner argues that her "offer specifie[d] the amount of [her] liability" because she offered "100% of the tax and the penalties" for years 2008, 2009, and 2010, and because her "liability in this case, without regard to innocent spouse relief, is less than what her liability would have been had [r]espondent accepted the offer." Petitioner's rationale for determining liability "without regard to innocent spouse relief" is that her offer "was made almost 2 years before she made innocent spouse relief an issue by pleading it as an affirmative defense in this deficiency proceeding." That is, because petitioner raised her section 6015 claim after submitting her offer, "such relief from liability is to be ignored for the purpose of determining whether [p]etitioner is treated as a prevailing party under the qualified offer provision of I.R.C. § 7430(c)(4)(E)." *See* Treas. Reg. § 301.7430-7(b)(3)

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[7] Respondent also argues that petitioner's offer was not a qualified offer because she failed to provide respondent with "the substantiation and legal and factual arguments necessary to allow for informed consideration" of her claim for relief from joint and several liability under section 6015, *see* Treas. Reg. § 301.74307(c)(4), because she did not file Form 8857 or otherwise provide information about her entitlement to relief from joint and several liability under section 6015. In the light of our holding under section 7430(g)(1)(B) and Treasury Regulation § 301.7430-7(c)(3) we need not address this additional argument.

(discussing treatment of adjustments raised subsequent to last qualified offer when calculating liability pursuant to the judgment). Petitioner emphasizes that her offer "reserved all collection rights including innocent spouse relief" and that "[w]hen the offer was made, [she] did not know if she would ever submit a request for § 6015 relief" because "[h]er husband . . . was in a position to pay the deficiency, potentially obviating the need for [her] to claim § 6015 relief."

III. *Petitioner's Offer*

Whether petitioner's offer is a qualified offer turns on whether reserving the right to claim relief under section 6015 relates to collection (as she tries to frame it) or to her underlying tax liability. That question is answered by the text of section 6015 itself.

Section 6015 provides relief from the general rule under section 6013(d)(3) that spouses filing joint federal income tax returns are jointly and severally liable for all taxes due. The operative provision in section 6015(b) provides that in certain circumstances, an individual "shall be relieved of liability for tax (including interest, penalties, and other amounts)"; likewise, section 6015(c) discusses treatment of an individual's "liability for any deficiency which is assessed with respect to the return." That is, section 6015 relieves a taxpayer from liability for tax, not just the collection of tax. Indeed, spousal defenses are listed separately from collection alternatives as a basis for challenging a proposed collection action under section 6330(d)(1). *See* §§ 6330(c)(2)(A)(i), (d), 6320(c). A taxpayer may also seek relief from joint and several liability on a joint return by raising the matter as an affirmative defense in a petition for redetermination invoking the Court's deficiency jurisdiction under section 6213(a) (as petitioner did here), *see Butler v. Commissioner*, 114 T.C. 276, 287–88 (2000), or by filing a so-called stand-alone petition challenging a notice of determination denying a claim of innocent spouse relief, *see* § 6015(e)(1)(A).

Petitioner's reply concedes that section 6015 provides relief from liability. She argues that we should calculate her liability pursuant to the decision to be entered in this case "without regard to innocent spouse relief" and ignore "such relief from liability" (thereby acknowledging that section 6015 would otherwise affect her liability), and states that her spouse's payment of the deficiency would have "obviated the need for [her] to claim § 6015 relief." She gives us no legal basis for ignoring her reservation of her right to claim such relief in the December 2016 offer letter. Rather, we must read her reservation as a caveat as to liability. Consequently, her offer flunks the requirement in section 7430(g)(1)(B) that the qualified offer "specif[y] the offered amount of the taxpayer's liability." An offer that reserves the right to claim relief under section 6015 does not "specif[y] the offered amount of the taxpayer's liability" because the amount of liability offered depends on potential—and reserved—application of section 6015 and cannot be determined until availability of section 6015 relief is considered (or reservation of the right to claim it is withdrawn).

Applying the regulations to petitioner's offer illustrates the problem. Petitioner offered to concede "100% of the tax and 100% of the penalties" for years 2008, 2009, and 2010, subject to a reserved right to claim relief from joint and several liability under section 6015. Respondent's acceptance of that offer would not "fully resolve the taxpayer's liability, and only that liability . . . for the type or types of tax and the taxable year or years at issue in the proceeding"—that is, petitioner's federal income tax liabilities for 2008, 2009, and 2010—because her tax liabilities might be (and were) reduced to zero after consideration of her reserved right to claim relief from joint and several liability under section 6015(c). *See* Treas. Reg. § 301.7430-7(c)(3).

Petitioner argues that the "differences between the amount of an assessment pursuant to a qualified offer and the amount that a taxpayer actually pays as a result of adjustments that are not at issue when the offer was made, do not affect the validity of a qualified offer." She points to Treasury Regulation § 301.7430-7(e) (example 4), which discusses whether a taxpayer may reduce the amount the taxpayer will pay pursuant to a qualified offer after the offer is accepted by the Commissioner by applying net operating loss carryovers. Petitioner states that "[a] future innocent spouse claim is similar to the carryback of net operating losses." But unlike net operating loss carryovers not in issue when an offer is made and applied after a qualified offer is accepted to reduce payment for the years in issue, the right to relief from liability under section

6015 that petitioner reserved in her offer affects the amount of her liabilities—the assessed deficiencies—for the years in issue; it is not merely a carryover item applied later to reduce payment.

We therefore conclude that an offer that reserves the right to claim relief from joint and several liability under section 6015 is not a qualified offer because it fails "to specif[y] the offered amount of the taxpayer's liability" under section 7430(g)(1)(B), and would not fully resolve the taxpayer's liability. *See* Treas. Reg. § 301.7430-7(c)(3). Petitioner's offer reserved the right to claim relief from joint and several liability under section 6015, and therefore she did not make a qualified offer under section 7430(g).

IV. *Substantial Justification*

Because petitioner did not submit a qualified offer, her request for litigation costs will fail if respondent's position was substantially justified.

The "position of the United States" in a Tax Court proceeding is that set forth in the Commissioner's answer. *See* § 7430(c)(7)(A); *Huffman v. Commissioner*, 978 F.2d at 1148; *Maggie Mgmt. Co. v. Commissioner*, 108 T.C. 430, 442 (1997). In his answer to petitioner's amended petition, respondent acknowledged that petitioner requested innocent spouse relief under section 6015 and stated that he "will review her request and make a determination regarding her eligibility for said relief."

A position is "substantially justified" if it is "justified to a degree that could satisfy a reasonable person" or has a "reasonable basis both in law and fact." *Swanson v. Commissioner*, 106 T.C. 76, 86 (1996) (quoting *Pierce v. Underwood*, 487 U.S. 552, 565 (1988)); *see also Huffman v. Commissioner*, 978 F.2d at 1147. The determination of reasonableness is based on all the facts of the case and the available legal precedents. *Maggie Mgmt. Co.*, 108 T.C. at 443. A position has a reasonable basis in fact if there is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion. *Underwood*, 487 U.S. at 565. A position has a reasonable basis in law if legal precedent substantially supports the Commissioner's position given the facts available to him. *Maggie Mgmt. Co.*, 108 T.C. at 443. Treasury Regulation § 301.7430-5(d)(1) provides:

> A significant factor in determining whether the position of the Internal Revenue Service is substantially justified as of a given date is whether, on or before that date, the taxpayer has presented all relevant information under the taxpayer's control and relevant legal arguments supporting the taxpayer's position to the appropriate Internal Revenue Service personnel.

Respondent's position was substantially justified because petitioner did not "present[] all relevant information under [her] control," *id.*, and respondent's position had a reasonable basis both in law and fact. A reasonable person could require information such as Form 8857 or other documentation supporting petitioner's claim for innocent spouse relief before making a determination. *See, e.g.*, I.R.S. Chief Counsel Notice CC-2013-011, 2013 WL 3148998 (June 7, 2013) (directing the Commissioner's counsel to seek a CCISO determination regarding relief under section 6015 in docketed cases with no prior CCISO review). The submission of Form 8857 or other supporting documentation to the Commissioner for CCISO review frequently has preceded evaluation of a claim for innocent spouse relief. *See, e.g., Knudsen v. Commissioner*, 793 F.3d at 1032; *Angle v. Commissioner*, T.C. Memo. 2015-92, at *3–4 *supplemented by* T.C. Memo. 2016-27, *aff'd*, 699 F. App'x 703 (9th Cir. 2017); *Estate of Lippitz v. Commissioner*, 2007 WL 2780496, at *2. And respondent ultimately conceded that relief was appropriate not on the basis of documentation petitioner submitted (there was none) but instead the settlement respondent reached with petitioner's former spouse.

V. *Conclusion*

In sum, petitioner is not a prevailing party under section 7430(c)(4) because she did not bear her burden of proving that she made a qualified offer and respondent bore his burden of proving that his position was substantially justified. We therefore will deny her motion for litigation costs.

An appropriate order and decision will be entered.

APTARGROUP INC., PETITIONER *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 7218-20. Filed March 16, 2022.

P owns stock in a controlled foreign corporation (CFC) that apportioned interest expense under the modified gross income method. P claimed a foreign tax credit under I.R.C. § 904 with respect to tax imposed on its income from the CFC. To determine the amount of the foreign tax credit, P characterized its stock in the CFC using the asset method. Thus, P did not use the same method that the CFC used for interest expense apportionment. R issued a notice of deficiency to P denying the foreign tax credit. The parties have filed Cross-Motions for Partial Summary Judgment on the issue of whether P must use the modified gross income method to characterize the stock of its CFC for purposes of computing the foreign tax credit as it is the method that the CFC used to apportion interest expense. *Held*: P's position is inconsistent with the proper application of Temp. Treas. Reg. § 1.861-9T(f)(3)(iv), which requires the U.S. shareholder of a CFC to characterize the stock of the CFC using the same method that the CFC used to apportion its interest expense and which is not limited by Temp. Treas. Reg. § 1.861-12T.

Robert E. Dallman, *John A. Sikora*, and *Courtney A. Hollander*, for petitioner.

Maha Sadek and *Naseem Jehan Khan*, for respondent.

OPINION

GOEKE, *Judge*: This case is before the Court on Cross-Motions for Partial Summary Judgment on the apportionment of interest expense with respect to petitioner's stock in a controlled foreign corporation (CFC) for purposes of the computation of a foreign tax credit. We will grant respondent's Motion and deny petitioner's Motion.

Background

There is no dispute as to the following facts, which are drawn from the Petition and the Stipulation of Facts. Petitioner is a U.S. corporation that filed a consolidated income tax return for 2014 and had its principal place of business in Illinois when it timely filed the Petition.

In December 2014 petitioner restructured its ownership of its foreign subsidiaries. Before the restructuring, petitioner directly owned 100% of AptarGroup Holdings, an entity organized under the laws of France (AGH France), which served as a global holding company for most of petitioner's foreign subsidiaries. Petitioner owned, directly or indirectly, 42 CFCs and also directly owned stock in other foreign corporations including noncontrolled foreign corporations as described in section 902.[1] As part of the restructuring, petitioner transferred ownership of substantially all of its foreign subsidiaries including AGH France to a Luxembourg holding company, AptarGroup Global Holding (AGH Lux). After the restructuring, petitioner wholly owned AGH Lux, which wholly owned, directly and indirectly, 32 CFCs. The CFCs held assets that generated foreign source income, and some also held assets that generated U.S. source income. Petitioner remained the direct owner of five CFCs.

During 2014 petitioner paid or accrued interest expense or was deemed to have done so. On its 2014 return petitioner claimed a foreign tax credit of $3,539,543. On February 27, 2020, respondent issued a notice of deficiency to petitioner for 2014 disallowing the foreign tax credit in its entirety and determining a deficiency of $3,539,543 and a section 6662(a) accuracy-related penalty. The parties have filed Cross-Motions for Partial Summary Judgment with respect to the method that petitioner may use to apportion interest expense for purposes of calculating the foreign tax credit.

Discussion

The purpose of summary judgment is to expedite litigation and avoid costly, unnecessary, and time-consuming trials. *FPL Grp., Inc. & Subs. v. Commissioner*, 116 T.C. 73, 74 (2001). We may grant partial summary judgment when there is no genuine dispute of material fact and a decision may be rendered as a matter of law. Rule 121(b); *see Fla. Peach Corp. v. Commissioner*, 90 T.C. 678, 681 (1988). The parties state that there is no genuine dispute of material fact affecting the method of interest expense apportionment, and we find no such dispute.

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[1] Unless otherwise indicated, all statutory references are to the Internal Revenue Code (Code), Title 26 U.S.C., in effect at all relevant times, all regulation references are to the Code of Federal Regulations, Title 26 (Treas. Reg.), in effect at all relevant times, and all Rule references are to the Tax Court Rules of Practice and Procedure.

The issue is solely a question of law. Accordingly, the issue may appropriately be adjudicated summarily.

I. *Foreign Tax Credit*

The United States taxes its citizens and domestic corporations on worldwide income. *See, e.g.*, *Cook v. Tait*, 265 U.S. 47, 56 (1924); *Huff v. Commissioner*, 135 T.C. 222, 230 (2010). Because this policy creates the potential for double taxation, the Code allows U.S. citizens and domestic corporations a credit for income tax paid to a foreign country. § 901(a); *Am. Chicle Co. v. United States*, 316 U.S. 450 (1942); *Vento v. Commissioner*, 147 T.C. 198, 203–04 (2016), *supplemented by* 152 T.C. 1 (2019), *aff'd*, 836 F. App'x 607 (9th Cir. 2021). A domestic corporation may also claim a credit for tax that it is deemed to have paid or accrued. § 960. The extent to which a taxpayer is entitled to a foreign tax credit is determined by applying U.S. tax law; thus, the source of income depends on how U.S. tax law categorizes such income. *United States v. Goodyear Tire & Rubber Co.*, 493 U.S. 132 (1989); *Phillips Petroleum Co. v. Commissioner*, 104 T.C. 256, 295 (1995).

The Code limits the amount of a foreign tax credit to prevent taxpayers from using foreign tax to reduce U.S. tax on their U.S. source income. *Theo. H. Davies & Co. v. Commissioner*, 75 T.C. 443, 446 n.9 (1980), *aff'd per curiam*, 678 F.2d 1367 (9th Cir. 1982). The allowable foreign tax credit for a taxable year is the lesser of foreign tax paid or accrued (or so deemed) or the foreign tax credit limitation (FTC limitation). § 904(a). The foreign tax credit is limited to "the same proportion of the tax against which such credit is taken which the taxpayer's taxable income from sources without the United States . . . bears to his entire taxable income for the same taxable year," and the FTC limitation is computed by multiplying total U.S. tax on worldwide income by a fraction with a numerator of foreign source taxable income and a denominator of worldwide taxable income. *Id.* Generally, in the case of an affiliated group of corporations, the foreign tax credit is determined on a consolidated basis. Treas. Reg. § 1.1502-4(c).

Where a taxpayer has more than one category of income as listed in section 904(d) (limitation category), the FTC limitation must be computed separately for each limitation category. § 904(d)(1). The FTC limitation is computed for the affiliated group, i.e., the totals for the affiliated group. Treas. Reg. § 1.1502-4(d). Petitioner earns income in more than one limitation category and must compute more than one FTC limitation. However, AGH Lux stock generates income from only one limitation category although it generates both foreign and U.S. source income.

II. *Sourcing Rules*

To compute the FTC limitation, the taxpayer must determine the source for its gross income. The sourcing rules are in the regulations under section 861, which are used in conjunction with operative sections of the Code, i.e., Code sections such as section 904 that require the taxpayer to determine taxable income from specific sources or activities. After determining the source of the gross income, the taxpayer must allocate each loss, expense, and other deduction (collectively, expense) to a class of gross income and then, if necessary, apportion the expense within the class of gross income between (or among) a statutory grouping and a residual grouping. *See* Treas. Reg. § 1.861-8(a)(2). A statutory grouping is gross income from the specific source or activity that is relevant for purposes of the operative section at issue, and the residual grouping is gross income from all other sources or activities. *Id.* subpara. (4). For purposes of the foreign tax credit, each limitation category is a statutory grouping, and a taxpayer claiming the credit must determine the foreign source taxable income in each limitation category in which it has income.

In general, expenses are allocated and apportioned on the basis of the factual relationship of the expense to gross income.[2] *Id.* subpara. (2). Expenses are allocated to the class of gross income to which they definitely relate. *Id.* para. (b)(1) and (2) (defining "definitely related"). Some expenses are not definitely related to a class of gross income or are related

[2] The gross income to which a specific deduction is factually related is referred to as a "class of gross income." Treas. Reg. § 1.861-8(b)(1). Classes of gross income are not predetermined; a taxpayer determines its classes of gross income on the basis of the deductions that it must allocate. *Id.* A class of gross income may consist of one or more items of gross income enumerated in section 61 such as compensation for services, gross income derived from business, interest, rents, royalties, dividends, or subdivisions of these items. Treas. Reg. § 1.861-8(a)(3). For allocation of interest expense, all the taxpayer's gross income is treated as one class.

to all gross income and thus must be ratably allocated to all gross income. *Id.* Next, if necessary, expenses are apportioned between the statutory and residual groupings. *Id.* para. (c)(3).

III. *Special Rules for Interest Expense*

Special rules exist for allocation and apportionment of interest expense in Temporary Treasury Regulation § 1.861-9T (section -9T).[3] In general, interest expense is treated as related to all income-producing activities and assets regardless of the specific purpose for the borrowing, on the general principle that money is fungible, borrowing frees up other funds for other purposes, and management has flexibility as to the source and use of funds. *Id.* para. (a). Thus, interest expense must be ratably allocated to all gross income. Allocation is not at issue. Petitioner must allocate its interest expense to all its income-producing assets and activities. The parties disagree over the apportionment of the interest expense.

Section -9T sets out two methods for apportioning interest: the asset method and the modified gross income method, described at paragraphs (g) and (j), respectively. Domestic corporations must use the asset method. *Id.* para. (f)(1)(i). CFCs are permitted to choose either method subject to certain consistency requirements. *Id.* subpara. (3).

As a domestic corporation, petitioner apportioned its interest expense using the asset method. That method requires taxpayers to apportion interest expense to the various statutory groupings on the basis of the average total value of assets assigned to each grouping for the year. *Id.* para. (g)(1). To apply the asset method, therefore, petitioner is required to divide the value of its assets among the relevant statutory groupings, a process the regulations define as "characterizing" the assets. *See id.* subparas. (1), (3). At issue is petitioner's method for characterizing its AGH Lux stock under these rules.

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[3] The relevant version of the Temporary Regulation was effective from July 16, 2014, to December 7, 2016. The version of Temporary Treasury Regulation § 1.861-12T (section -12T) at issue was effective from August 4, 2009, to June 20, 2019.

IV. *Asset Characterization*

Section -9T(g)(3) sets out general asset characterization rules for purposes of applying the asset method. However, the regulations also provide a special consistency rule regarding the characterization of CFC stock in the hands of any U.S. shareholder. Specifically, section -9T(f)(3)(iv) provides: "Pursuant to [section -12T(c)(2)], the stock of a controlled foreign corporation shall be characterized in the hands of any United States shareholder using the same method that the controlled foreign corporation uses to apportion its interest expense."[4]

Section -12T(c)(3) describes two methods for characterizing CFC stock, which are referred to as the asset method and the modified gross income method, and imposes the same consistency rule. That rule provides as follows:

> Stock in a controlled foreign corporation whose interest expense is apportioned on the basis of assets shall be characterized in the hands of its United States shareholders under the asset method described in paragraph (c)(3)(ii). Stock in a controlled foreign corporation whose interest expense is apportioned on the basis of gross income shall be characterized in the hands of its United States shareholders under the gross income method described in paragraph (c)(3)(iii).

Section -12T(c)(3)(i) (flush text).

AGH Lux elected to apportion interest expense using the gross income method, as it was entitled to do under section -9T(f)(3)(i). But in characterizing its AGH Lux stock, petitioner did not apply the special characterization rules of sections -9T(f)(3)(iv) and -12T(c)(3) that require consistency. Rather, petitioner relied on the general characterization rules of section -9T(g)(3). This choice allowed petitioner to reduce the amount of interest expense that it apportioned to foreign source income thereby increasing its foreign source taxable income and increasing its foreign tax credit.

Respondent argues that petitioner is not permitted to use the general characterization rules because sections -9T(f)(3)(iv) and -12T(c)(3)(i) required it to characterize its stock in AGH Lux using the modified gross income method described in section -12T(c)(3)(iii). Petitioner disagrees, arguing that sections -9T(f)(3)(iv) and -12T(c)(3)(i) do not apply on the facts of this

[4] The reference to paragraph (c)(2) appears to be a typo; section -12T(c)(3) describes the characterization of CFC stock.

case, and therefore, it was free to characterize its AGH Lux stock using the general asset characterization rules of section -9T(g)(3). For the reasons below, we agree with respondent.

We interpret regulations using canons of statutory construction, begin with the text of the regulation, and give effect to its plain meaning. *See Austin v. Commissioner*, 141 T.C. 551, 563 (2013). To determine the plain meaning, we must look to the text at issue as well as the text and design of the regulation as a whole. *K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 291 (1988). "We interpret . . . regulations in toto rather than phrase by phrase." *Microsoft Corp. v. Commissioner*, 115 T.C. 228, 248–49 (2000) (citing *Norfolk Energy, Inc. v. Hodel*, 898 F.2d 1435, 1442 (9th Cir. 1990)), *rev'd and remanded*, 311 F.3d 1178 (9th Cir. 2002). A regulation should be interpreted so as to avoid conflict with the statute. *Phillips Petroleum Co. v. Commissioner*, 97 T.C. 30, 35 (1991), *aff'd without published opinion*, 70 F.3d 1282 (10th Cir. 1995). If a regulation is ambiguous, we must interpret the regulation in a manner that is "most harmonious with its scheme and with the general purposes." *NLRB v. Lion Oil Co.*, 352 U.S. 282, 297 (1957) (Frankfurter, J., concurring in part).

We begin by looking at the text of the relevant parts of the temporary regulations. Section -9T(f)(3) provides the CFC an election between the asset and the modified gross income methods, imposes the consistency requirement for purposes of interest expense apportionment in subdivision (iv), and refers to section -12T.

Section -9T(g)(1) describes the asset method and refers to paragraph (g)(3)(i) of that section and section -12T for asset characterization rules, providing as follows:

> Under the asset method, the taxpayer apportions interest expense to the various statutory groupings based on the average total value of assets within each such grouping for the taxable year, as determined under the asset valuation rules of this paragraph (g)(1) and paragraph (g)(2) of this section and the asset characterization rules of paragraph (g)(3) of this section and [section -12T].

Section -9T(f), after setting forth the asset method as the general rule, allows a CFC to elect to use the modified gross income method and expressly states the consequences of the election, that the U.S. shareholder of a CFC must characterize the CFC stock using the same method that the CFC used to apportion interest expense. Thus, under section -9T(f) the CFC's election of the modified gross income method binds the U.S. shareholder to that method. Petitioner argues that the modified gross income method is an exception to the consistency requirement. When we read section -9T(f)(3) in its entirety, it is clear that the election is not an exception. Rather, the consistency requirement is a condition of the election. The modified gross income method is an exception to the general rule of the asset method and is the reason for the consistency requirement. The consistency requirement is imposed because an election is provided.

Moreover, we disagree with petitioner that section -12T is determinative with respect to whether consistency is required on the facts here. Significantly, section -9T(f)(3)(iv) imposes the consistency requirement. That provision provides the rule, and section -12T is intended to supplement section -9T, including the consistency requirement that it imposes. We do not read the reference to section -12T in section -9T(f)(3)(iv) as limiting the application of the consistency requirement as petitioner suggests. Rather, it refers to section -12T as providing supplemental rules for the characterization of CFC stock. Section -9T(g)(1) and (3) also refers to section -12T as supplementing the rules contained therein. This conclusion is confirmed by section -9T(f)(4)(iii), which similarly cited section -12T(c) to establish a parallel rule for characterizing the stock of noncontrolled section 902 corporations. *See also* Treas. Reg. § 1.861-12(c)(4); section -12T(c)(4). Finally, section -9T(j), which describes the modified gross income method, states that it applies "[s]ubject to rules set forth in paragraph (f)(3)," reenforcing that use of the modified gross income method is subject to the consistency requirement.

Moreover, while petitioner argues that the introductory sentence of section -12T(a) excuses it from the consistency requirements of section -9T, section -12T(a) provides that "[t]hese rules are applicable to taxpayers in apportioning expenses under an asset method to income in various separate limitation categories under section 904(d), and supplement other rules provided in [sections -9T], 1.861-10T, and 1.861-11T." The concluding part of that sentence, "supplement other rules," establishes an additional purpose of the section -12T rules independent of section 904(d) apportionment. In 2019 the Secretary amended section -12T to clarify that it applies for all operative sections, not just section 904(d). *See* T.D. 9882, 84 Fed. Reg. 69022, 69070 (Dec. 17, 2019).

To summarize, we interpret the version of section -12T in effect for petitioner's 2014 taxable year. First and most significant, the consistency requirement of section -9T(f)(3)(iv) does not depend on whether section -12T applies. It imposes an independent consistency requirement for purposes of interest expense apportionment by a CFC that elected to use the modified gross income method. Furthermore, we do not agree that section -12T on its face provides the limitation that petitioner seeks. It is intended to supplement other rules including the section -9T provisions at issue here.

Petitioner's position is inconsistent with the proper application of section -9T. AGH Lux elected to use the modified gross income method to apportion interest expense; thus, petitioner must characterize its AGH Lux stock using the modified gross income method.

We have considered all other arguments made by the parties, and to the extent not discussed above find the arguments to be irrelevant, moot, or without merit. To reflect the foregoing,

An appropriate order will be issued.

BATS GLOBAL MARKETS HOLDINGS, INC. AND SUBSIDIARIES, PETITIONER *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 1068-17. Filed March 31, 2022.

P, an operator of national securities exchanges, charged its customers certain fees in connection with their participation on the exchanges (Fees). P developed computer software that it used to operate the exchanges. P treated the gross receipts from the Fees as domestic production gross receipts (DPGR) for the purpose of calculating deductions pursuant to I.R.C. § 199, which it claimed with respect to years 2011–13. R determined that none of the gross receipts from the Fees were DPGR. Under the applicable regulations, a taxpayer is entitled to treat as DPGR gross receipts derived from providing customers access to computer software for the customers' direct use. Treas. Reg. § 1.199-3(i)(6)(iii). Further, a third party must derive gross receipts from the disposition in a tangible medium or by download of substantially identical software (as compared to the taxpayer's software) to its customers. *Id.* subdiv. (iii)(B). *Held*: P is not entitled to treat the gross receipts from the Fees as DPGR under Treas. Reg. § 1.199-3(i)(6)(iii) because the Fees were not derived from providing customers access to computer software for their direct use. *Held*, *alternatively*, P is not entitled to treat the gross receipts from the Fees as DPGR because the third-party software proposed as comparable by P was not substantially identical software as compared to P's software. *See id.* subdiv. (iii)(B).

Mario J. Verdolini, Jr., *Christopher A. Baratta*, and *Lara S. Buchwald*, for petitioner.

Andrew Michael Tiktin, *M. Jeanne Peterson*, *Tatiana Belenkaya*, *David B. Flassing*, *Henry C. Bonney*, and *Erin H. Stearns*, for respondent.

KERRIGAN, *Judge*: Respondent issued a notice of deficiency determining deficiencies of $932,713, $1,319,418, and $1,425,984 for tax years 2011, 2012, and 2013 (years in issue), respectively. Petitioner timely sought redetermination in this Court. After concessions the issue for consideration is whether petitioner's transaction fees, routing fees, and logical port fees (collectively, Fees) qualify as domestic production gross receipts (DPGR) for the purpose of calculating deductions pursuant to section 199.

Unless otherwise indicated, all statutory references are to the Internal Revenue Code, Title 26 U.S.C., in effect at all relevant times, all regulation references are to the Code of Federal Regulations, Title 26 (Treas. Reg.), in effect at all relevant times, and all Rule references are to the Tax Court Rules of Practice and Procedure. We round all monetary amounts to the nearest dollar.

On December 16, 2019, the Court issued a protective order to prevent disclosure of petitioner's proprietary and confidential information. The facts and opinion have been adapted accordingly, and information set forth herein is not proprietary or confidential.

FINDINGS OF FACT

I. *Overview of Bats Global*

BATS Global Markets Holdings, Inc. (Bats Global), is, and was during the years in issue, a Delaware corporation with its principal place of business in Lenexa, Kansas. During the years in issue Bats Global was named BATS Global Markets, Inc., and owned 100% of BATS Exchange, Inc., BATS Y-Exchange, Inc., and BATS Trading, Inc. Bats Global was the common parent of a group of corporations (collectively, petitioner) which filed consolidated U.S. federal income tax returns for the years in issue. On February 28, 2017, petitioner became a subsidiary of Cboe Global Markets, Inc.

Bats Global was founded in mid-2005. "BATS" was an acronym of "Better Alternative Trading System." The name referred to an alternative trading system, a type of venue for matching buyers and sellers of securities that is subject to regulation different from that of a national securities exchange. *See* 17 C.F.R. § 242.300(a) (2009). Petitioner initially operated an alternative trading system. By the years in issue its exchanges were registered as national securities exchanges.

From mid-2005 through January 2006, petitioner's founders wrote software code for the trading of equity securities. In 2006 petitioner launched a trading platform using the software it had developed. By the end of 2007 petitioner had developed its trading platform software to allow for the trading of all U.S. equity securities. By the years in issue petitioner had become the third-largest operator of equities exchanges in the United States after NYSE Euronext and NASDAQ OMX Group, Inc.

During the years in issue petitioner developed and operated electronic markets for the trading of listed cash equity securities in the United States and Europe and listed equity options in the United States. It did not have any physical location where buyers and sellers could meet to engage in trading. In the years in issue petitioner had 85 to 108 employees, who were divided into the following departments: business development and marketing; communications; compliance, surveillance and membership services; corporate and legal; finance; human resources; infrastructure; operations; sales; and software development.

Petitioner operated two marketplaces for purchasers and sellers of securities: BATS Exchange (BZX) and BATS Y-Exchange (BYX). BZX and BYX targeted different market segments by offering different pricing structures. Petitioner also operated a marketplace for trading listed equity options as part of BZX, referred to as BATS Options.

II. *Regulation of the Exchanges*

BZX, BYX, and BATS Options (collectively, Exchanges) were registered with and regulated by the U.S. Securities and Exchange Commission (SEC) during the years in issue. The SEC had primary responsibility for enforcing the federal securities laws and regulations and could prohibit exchanges that violated the law from operating.

The Exchanges were treated as national securities exchanges pursuant to the Securities Exchange Act of 1934 (1934 Act), ch. 404, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a–78pp (2012)). A national securities exchange is defined as any exchange registered pursuant to 15 U.S.C. § 78f. 17 C.F.R. § 242.600(b)(45) (2005).

In 2006 petitioner launched the predecessor to BZX, an exchange that used maker-taker pricing. *See infra* Section V.B.3. Transaction Fees. Petitioner launched BATS Options as part of BZX in 2010. BATS Exchange, Inc., was responsible for regulatory filings with respect to BZX and BATS Options. The SEC approved the application of BZX to register as a national securities exchange on August 18, 2008, and trading commenced on October 24, 2008. The SEC approved BATS Options as part of BZX on January 26, 2010, and trading commenced on October 15, 2010.

In 2010 petitioner launched BYX, an exchange that used taker-maker pricing. *See infra* Section V.B.3. Transaction Fees. BATS Y-Exchange, Inc., was responsible for regulatory filings with respect to BYX. On August 13, 2010, the SEC approved the application of BYX to register as a national securities exchange, and trading commenced on October 15, 2010.

A. *Securities Exchange Act of 1934*

For the Exchanges to be designated national securities exchanges, certain statutory requirements needed to be met. *See* 15 U.S.C. § 78f(b). A national securities exchange must comply with the 1934 Act and be able to enforce compliance by its members and persons associated with its members. Petitioner was required to ensure that quotation information supplied to investors and the public was fair and informative, and not discriminatory, fictitious, or misleading.

The SEC reviewed the Exchanges to ensure that they had the capacity to carry out the purposes of the 1934 Act. Upon granting the Exchanges' applications to register as national securities exchanges, the SEC found that the Exchanges' rules were designed to facilitate transactions in securities, promote just and equitable principles of trade, prevent fraudulent and manipulative acts and practices, and protect investors and the public interest.

Regulations under the 1934 Act specify that the exchange itself "[b]rings together the orders for securities of multiple buyers and sellers" and "[u]ses established, non-discretionary methods (whether by providing a trading facility or by setting rules) under which such orders interact with each other, and the buyers and sellers entering such orders agree to the terms of a trade." 17 C.F.R. § 240.3b-16(a) (2005). Under the 1934 Act an "exchange" means

> any organization, association, or group of persons, whether incorporated or unincorporated, which constitutes, maintains, or provides a market place or facilities for bringing together purchasers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange as that term is generally understood, and includes the market place and the market facilities maintained by such exchange.

15 U.S.C. § 78c(a)(1). The term "facility" includes an exchange's

> premises, tangible or intangible property whether on the premises or not, any right to the use of such premises or property or any service thereof for the purposes of effecting or reporting a transaction on an exchange (including, among other things, any system of communication to or from the exchange, by ticker or otherwise, maintained by or with the consent of the exchange), and any right of the exchange to the use of any property or service.

15 U.S.C. § 78c(a)(2).

B. *Regulation National Market System*

Petitioner's Exchanges were also subject to the Regulation National Market System (Regulation NMS), a set of rules promulgated by the SEC in 2005. 70 Fed. Reg. 37,496 (June 29, 2005); 17 C.F.R. §§ 242.600–242.612 (2005). For example, the Regulation NMS limited petitioner's transaction fees to a specified amount or percentage per share. 17 C.F.R. § 242.610(c).

Another of the rules set forth in the Regulation NMS is the order protection rule, which generally does not permit national securities exchanges to execute customers' orders at a price other than the best available ask price when buying securities and the best available bid price when selling securities (also known as the national best bid or offer, or NBBO). 17 C.F.R. § 242.611; *see also id.* § 242.600(b)(42) (defining NBBO). A bid is an order to buy at a certain price and an offer is an order to sell at a certain price. *See* 17 C.F.R. § 242.600(b)(8). The term "order" means "any firm indication of a willingness to buy or sell a security, as either principal or agent, including any bid or offer quotation, market order, limit order, or other priced order." *Id.* § 240.3b-16(c). For purposes of the Regulation NMS the best bid and best offer mean the highest priced bid and the lowest priced offer. *Id.* § 242.600(b)(7). If a competing exchange has a better price than that offered on the exchange that received the order, the order must be routed to the exchange with the better price.

To ensure compliance with the order protection rule, petitioner's trading software was coded so that there could not have been executions on the Exchanges without the market data from the consolidated tape reflecting the NBBO on other registered exchanges. The consolidated tape was generated by securities information processors operated by NASDAQ and a subsidiary of NYSE.

III. *Bats Global Customers*

Petitioner's customers were organizations that were members of either BATS Exchange, Inc., or BATS Y-Exchange, Inc. In addition, members were able to sponsor their own customers to participate in trading on the Exchanges.

To become a member, a prospective customer was required to be registered as a broker-dealer with the SEC, be a member of at least one other national securities exchange or national securities association, be able to clear trades on its own or through a clearing firm, and meet additional prescribed criteria. During the years in issue prospective customers were required to fill out a membership application and to execute a user agreement and a securities routing agreement. There were no membership fees payable to petitioner. Members did not become stockholders of BATS Exchange, Inc., or BATS Y-Exchange, Inc.

Some of petitioner's customers were broker-dealers affiliated with separate entities, such as banks, that operated their own electronic markets. These broker-dealers may have routed orders from their affiliates' electronic markets to the Exchanges. Petitioner's trading software would have received, handled, and processed orders routed to petitioner's Exchanges in the same way as orders from any of petitioner's other customers.

A member of BATS Exchange, Inc., could also be authorized to become an options member and transact business on BATS Options. To become an options member, a BATS Exchange, Inc., member had to complete a separate application and an options member agreement.

A. *Exchange Rules*

By signing the membership application, a potential member agreed to abide by the rules of the relevant exchange (Exchange Rules) and "to pay such dues, fees, assessments, and other charges in the manner and amount as shall from time to time be fixed by the exchange." Sponsored participants also agreed to abide by the Exchange Rules and executed a separate user agreement and a securities routing agreement with petitioner.

Exchange Rule 15.1 stated with respect to the fees of the Exchanges:

> Rule 15.1 Authority to Prescribe Dues, Fees, Assessments, and Other Charges
>
> (a) Generally. The Exchange may prescribe such reasonable dues, fees, assessments or other charges as it may, in its discretion, deem appropriate. Such dues, fees, assessments, and charges may include membership dues, transaction fees, communication and technology fees, regulatory charges, listing fees, and other fees and charges as the Exchange may determine. All such dues, fees and charges shall be equitably allocated among Members, issuers, and other persons using the Exchange's facilities.
>
> . . . .

> (c) Schedule of Fees. The Exchange will provide Members with notice of all relevant dues, fees, assessments, and charges of the Exchange. Such notice may be made available to Members on the Exchange's website or by any other method deemed reasonable by the Exchange.

The Exchange Rules governed how the Exchanges operated, including how customers' orders were handled and matched and how members were regulated. Exchange Rule 11.3 stated with respect to customers' access to the Exchanges:

> Rule 11.3. Access
>
> (a) General. The System shall be available for entry and execution of orders by Users with authorized access. To obtain authorized access to the System, each User must enter into a User Agreement with the Exchange in such form as the Exchange may provide ("User Agreement").

The Exchange Rules defined petitioner's "System" as "the electronic communications and trading facility designated by the Board through which securities orders of Users are consolidated for ranking, execution, and when applicable, routing away."

B. *The User Agreement*

The user agreement executed by petitioner and each customer provided that customers had the right to receive certain services from petitioner. The user agreement explained the services as follows:

> 2. Services. Subject to the terms and conditions of this Agreement, User will have the right to access Exchange to enter orders on Exchange, receive status updates on orders, cancel orders, execute trades against orders on the Exchange limit order book and to receive data feeds from Exchange ("Exchange Data") containing information regarding User's open orders, executions and volume on Exchange (collectively, the "Services").

The user agreement explained that customers could be charged system usage fees as follows:

> 13. Fees. By signing this Agreement, User agrees to make timely payment of all system usage fees, as may be set forth in Exchange Rules or posted on Exchange's web site.

C. *The Securities Routing Agreement*

Petitioner executed a securities routing agreement with each customer providing that petitioner's subsidiary, BATS

Trading, Inc., routed customers' orders to marketplaces outside of the Exchanges. BATS Trading, Inc., was a registered broker-dealer and was able to submit orders to external markets, such as the New York Stock Exchange or NASDAQ, which required members to be broker-dealers.

The securities routing agreement was governed and interpreted in accordance with New York law. It provided as follows:

> Provided that User is a Member or Sponsored Participant of a Member of [the relevant exchange] and subject to a valid, ongoing User Agreement with Exchange, BATS Trading, Inc. (hereinafter "BATS Trading"), a broker-dealer registered in accordance with Section 15(a) of the Securities Exchange Act of 1934, as amended (the "Act"), agrees to act as agent to User for the purpose of providing certain routing services, as described herein, provided that User is bound by the terms and conditions of this agreement (the "Routing Agreement") and any applicable rules and interpretations of Exchange Rules. Whereas BATS Trading provides certain order routing services for Exchange, and User desires to use the order routing facilities of Exchange, for good and valuable consideration, User and BATS Trading agree as follows:
>
> 1. Routing Services. BATS Trading, a wholly owned subsidiary of BATS Global Markets, Inc., agrees to act as agent for User for routing orders into Exchange to the applicable market centers or broker-dealers for execution, whenever such routing is at User's request, and is permitted in accordance with Exchange Rules. User understands and agrees that orders executed on its behalf shall at times be subject to the terms and conditions of Exchange Rules.

BATS Trading also entered into separate agreements with third-party routing companies, such as Bank of America, Merrill Lynch, Citi and affiliates of Citi, Morgan Stanley, Credit Suisse, and Lime Brokerage, under which these companies routed customers' orders to external markets on behalf of BATS Trading. BATS Trading, Inc., paid the transaction fees, connectivity fees, and membership fees charged by the external exchanges.

D. *Market Makers*

The Exchange Rules allowed members to register as market makers in one or more securities traded on the Exchanges. Market makers provided liquidity to the Exchanges by continuously submitting both bids and offers for one or more securities to the Exchanges' order books during regular trading hours.

IV. *Overview of Electronic Trading Platforms*

Historically, securities exchanges operated physical locations where stocks were bought and sold, known as trading floors. On these trading floors brokers and dealers physically found each other in order to make trades. Employees of the securities exchanges provided a variety of services to customers to support their trading, such as recording information about trades and helping brokers on the trading floor communicate with their business teams.

Beginning in the late 1990s and early 2000s the traditional model of in-person trading at a single physical location was replaced by that of computerized trading. By 2004 the volume of electronic trading exceeded that of in-person trading.

In an electronic market, buy and sell orders are matched with the use of technology, normally without any human intervention by the market's operator. Electronic trading platforms allow buy and sell orders to be matched according to a variety of strategies and trades to be executed at high speeds.

The operators of trading venues can use electronic trading platforms in a variety of ways beyond making them available for their members to trade. Operators of trading venues can use electronic trading platforms to operate their markets, including to choose what instruments (e.g., equities, commodities, and options) can be traded on their markets; to choose what order types their markets will accept; to determine who can submit orders to their markets; to cancel erroneous trades; to control whether their markets are open or shut down; to modify the matching engine software so that the matching logic implements the rules of their markets; to electronically disseminate market data to customers; and to receive real-time market information necessary for order execution.

V. *Operation of the Exchanges*

Petitioner's Exchanges matched the orders of buyers and sellers, functioned as sources of liquidity to petitioner's customers, and provided customers with fair and orderly places to trade. Petitioner's customers submitted orders to the Exchanges, and petitioner provided matching and trade execution services.

During the years in issue the Exchanges' hours of operation were 8 a.m. to 5 p.m. ET Monday through Friday, except for trading holidays. Orders were rejected if they were received outside the hours of operation. Those orders remaining after hours were canceled automatically.

The number of trades executed on BZX was 951,452,396 in 2011, 747,146,823 in 2012, and 681,854,332 in 2013. The number of trades executed on BYX was 266,234,530 in 2011, 292,853,247 in 2012, and 184,728,242 in 2013. These figures do not include executions of trades of fewer than 100 shares, referred to as "odd lot" trades.

Petitioner maintained two customer support departments, the Trade Desk and the Network Operations Center. The Network Operations Center focused on network operations, including customer connectivity and connectivity troubleshooting, and provided secondary support to the Trade Desk. The Trade Desk communicated with customers about the behavior of order types, provided simple connectivity troubleshooting support, coordinated market data requests, informed customers of system updates, assisted with logical port configuration, and certified order entry systems. The Trade Desk could also cancel customer orders. During the years in issue the Trade Desk received approximately 50 to 100 emails and 20 to 40 telephone calls a day from customers requiring assistance.

A. *Trading Software*

Petitioner developed software that was used in effecting the trading of securities and options on the Exchanges. The Exchanges did not operate solely through the use of petitioner's trading software but also incorporated third-party software, such as market surveillance software licensed from SMARTS. In developing its trading software, petitioner used Linux operating system software and other open-source software, which petitioner did not develop. Customer orders could not have been executed without this third-party software.

All software requires hardware to run. Online software hosted on the internet commonly uses interconnected software modules operating on interconnected computer hardware. Consistent with this model, petitioner's trading software was installed on interconnected computer servers in a data center in New Jersey that petitioner leased from a third party. Petitioner also maintained a backup data center for disaster recovery purposes.

Petitioner's computers in the data centers were interconnected to each other and to networking devices such as routers and switches. A computer network is two or more computers that are linked together to allow information sharing, resource sharing, or electronic communication. Petitioner purchased all the hardware used in its system from outside vendors and did not develop the operating system software used on the computers in its network.

To trade on the Exchanges, exchange members needed both "physical" connectivity and "logical" connectivity to petitioner's system. Customers established physical connectivity by placing their own computer hardware in petitioner's data center and using a cable to connect their computer hardware to petitioner's computer hardware. For part of the years in issue, petitioner charged customers a monthly physical connection fee for this wired connection.

Customers established logical connectivity by sending specially formatted electronic messages from order management software on their computers to logical ports in petitioner's system. A "logical port," as used in the computing industry, means a combination of a specific Internet Protocol (IP) address of a server and a Transmission Control Protocol (TCP) port, a unique number used to identify a location where data is to be sent. A TCP/IP port is not application software. Together, an IP address and a TCP port number allow a connection to be established between the application software on the computer of the person sending data and a particular instance of the target application software on another computer system.

Order management software was the means by which customers were able to connect with the Exchanges. Petitioner did not develop the order management software that customers used to establish and maintain the logical connection. Customers paid petitioner a monthly logical port fee in relation to this connection.

Petitioner's trading software was not downloaded to customers' computers or transferred to the random-access memory in customers' computers. Customers did not enter into license agreements with petitioner. Petitioner did not make copies of any portion of its trading software commercially available to third parties or offer it on a tangible medium or as a hosted arrangement for customers operating an electronic market. Petitioner's customers were unable to use any of the BATS trading software to operate their own exchange or similar market.

Petitioner's trading software comprised a variety of software applications, including the following: (1) the order handler, (2) the matching engine, (3) the routing engine, and (4) multicast PITCH feed servers. Multiple instances of these applications ran on petitioner's computers at one time. The order handler received customers' orders, validated orders, accepted or rejected the orders, and upon acceptance of an order converted the order to a proprietary format before relaying the order to the appropriate matching engine.

Customers were limited in their interactions with petitioner's trading system. They could submit new orders, send requests to modify existing orders or cancel orders resting on the order book, and receive messages regarding the status of their orders. Petitioner also provided customers access, at no charge, to a web portal on which they could adjust the default settings of the order handler software. For example, customers could restrict their ability to submit certain types of orders or set maximum per-order limits. Customers could also select the order handling option of "display price sliding," through which the displayed price of their orders would be adjusted according to the NBBO, allowing them to obtain a better price on purchase or sale of the security. The order handler applications generated electronic messages that were sent back to customers to inform them of the status of their orders.

Customers sent orders to the order handler using either the Financial Information Exchange (FIX) protocol, with specific modifications by BATS, or petitioner's proprietary protocol, the binary order entry (BOE) protocol. Instances of the order handler application were programmed to use either the FIX protocol or the BOE protocol. Each instance of the FIX order handler application was programmed to receive up to 5,000 electronic messages per second. Instances of the BOE order handler application were also generally subject to the same restriction. The purpose of these limits was to protect the matching engine from destabilizing because of excessive use. The BOE order handler application also had bulk quoting capabilities for trading on BATS Options, allowing users to send an increased number of orders per second.

The matching engine matched customers' buy-side and sell-side orders. Customers did not match their own orders. As provided by U.S. securities law, the Exchanges were responsible for bringing together customer orders. *See* 17 C.F.R. § 240.3b-16(a)(1).

The matching engine applied a time stamp to each order recording the time at which the order arrived in the matching engine or was last modified by the user. In general orders were continuously and automatically matched pursuant to price/time priority, under which priority was given to the best-priced orders in the order in which they arrived on the order book. The best-priced orders were determined using market data about the NBBO from external markets. If the matching engine could not match an order with those resting on the relevant exchange's relevant order book, it had the functionality to cancel the order or to send the order to the routing engine to be routed to another trading venue.

The routing engine routed a customer's orders, according to the customer's instructions, to one or more external markets, such as the New York Stock Exchange or NASDAQ, for potential execution. The routing engine could send an order to multiple external markets at virtually the same time by splitting it into smaller pieces, called child orders. The routing engine contained a software process that converted customer's orders into a form that would be accepted by the external markets.

The multicast PITCH feed server provided customers with a data feed of orders and executions on the Exchanges. The multicast PITCH server would read the outputs of the matching engine and send anonymized data about order executions and orders displayed on the order book of the relevant exchange to customers. To receive market data from the multicast PITCH server, customers needed to obtain and connect to a PITCH port or a multicast PITCH spin server port offered by petitioner. Petitioner provided some data feeds to customers for free but charged fees for others. Customers did not have to be members of the Exchanges to receive market data.

B. *The Fees*

Petitioner published fee schedules that governed the payments required of petitioner's customers. The fee schedules did not include the word "software."

Petitioner claimed as DPGR the receipts from the following three categories of fees it charged its customers: logical port fees, routing fees, and transaction fees. The following table displays petitioner's receipts from logical port fees, routing fees, and transaction fees during each of the years in issue

Item	*2011*	*2012*	*2013*
Logical port fees	$18,485,900	$25,879,850	$31,640,000
Routing fees	76,882,265	57,551,699	48,885,718
Transaction fees	590,490,229	515,179,765	494,944,299
Total	**685,858,394**	**598,611,314**	**575,470,017**

1. *Logical Port Fees*

Customers paid fixed monthly fees for logical connectivity to certain ports, referred to in petitioner's fee schedules as "logical ports" (described by petitioner as "FIX ports" and "BOE ports"). On its Forms S–1, Registration Statement Under the Securities Act of 1933, filed with the SEC, petitioner stated that these logical port fees represented fees paid for connectivity to its markets.

Each logical port was configured by petitioner to be able to handle a certain number of orders up to 5,000 messages per second. The messages customers could submit were new orders, requests to modify existing orders, and requests to cancel orders resting on the order book. If customers wanted to submit more than 5,000 messages per second or to send more than one order in parallel, they could pay to connect to more than one logical FIX port or BOE port, as needed for their order flow. Customers paid the same flat monthly fee for connectivity to each of these ports regardless of whether they submitted zero orders or the maximum number of orders per second.

Petitioner also offered ports with bulk quoting capabilities, which imposed no limit on the number of messages submitted per second. These ports were specific to BATS Options and carried a higher fee than the logical ports with limits on the number of messages sent per second.

2. *Routing Fees*

Petitioner charged routing fees to customers when orders that had been routed to other exchanges or trading venues were executed. Petitioner charged a routing fee only when there was an execution on an external market. When customers made an order, they specified whether the order should be filled on the Exchanges or routed to other exchanges, such as the New York Stock Exchange or dark pools. Dark pools are marketplaces that allow their users to place orders without publicly displaying the size and price of their orders to other participants in the dark pool.

Routing fees were charged to customers using the Exchanges according to the number of shares or option contracts routed to another exchange and the routing strategy used. The fee per share or option contract executed varied with the strategy the customer selected.

Customers were able to select from a variety of strategies for how their orders would be routed to external markets. For example, customers could choose to have their orders routed only to particular types of marketplaces, such as only to dark pools. Customers could also select strategies that prioritized factors such as price or likelihood of execution.

3. *Transaction Fees*

The primary source of petitioner's revenues was its transaction fees. When a customer's order was executed, the customer was either charged a transaction fee or issued a rebate. Petitioner referred to the transaction fees as "Fees for Accessing Liquidity" or "Liquidity Fees" on the fee schedules for BZX and BYX, respectively. The rebates for customers on the opposite side of these executions were referred to as "Liquidity Rebates" or "Rebates for Accessing Liquidity" on BZX and BYX, respectively. Petitioner's fee schedules provided that petitioner charged a customer a transaction fee or issued a customer a rebate for each share executed that, depending on the exchange, added liquidity to or removed liquidity from the order book.

Liquidity refers to the ability of market participants to buy and sell securities. Generally, the more orders available in a market, the greater the liquidity. In the context of petitioner's Exchanges, liquidity referred to the number and price range of orders resting on the Exchanges' order books that were available to be matched with other orders. Petitioner derived liquidity from orders to buy or sell that customers submitted to the Exchanges electronically. Petitioner offered rebates as an incentive to attract market participants and liquidity to the Exchanges.

Whether a customer was charged a fee or issued a rebate depended on which of the Exchanges the customer was trading on and whether the customer's order was immediately executable when entered. Orders that were not immediately executable when entered were posted on the order book, referred to as adding liquidity. Orders that were immediately executable when entered were referred to as taking, or removing, liquidity. Petitioner generated revenue from the difference between the fees charged to customers and the rebates issued to customers. The following table displays the transaction fees petitioner received and the rebates petitioner paid customers during each of the years in issue:

Item	*2011*	*2012*	*2013*
Transaction fees	$695,357,000	$645,310,000	$612,806,000
Rebates	566,103,000	508,169,000	474,688,000

BZX and BATS Options issued rebates for adding liquidity and charged fees for taking liquidity, referred to as a "maker-taker" pricing model. The maker-taker pricing model used by BZX was designed to incentivize market makers to provide liquidity on a continuous basis. Besides the rebate for adding liquidity, market makers were eligible to receive an additional daily rebate on BZX if they satisfied a daily quoting requirement.

BYX charged fees for adding liquidity and issued rebates for removing liquidity, referred to as a "taker-maker" pricing model. Petitioner issued rebates as a financial incentive for customers to prioritize BYX over other markets for their liquidity removal orders.

The price customers were charged per share varied with the type of order the customer submitted. A wide range of order types was available to customers, including market orders, limit orders, reserve orders, discretionary orders, peg orders, and hidden orders. Hidden orders allowed a customer to hide all or a portion of its order from display in market data and on the order book. Petitioner charged different prices for hidden orders compared to orders that were displayed. On BYX petitioner charged higher prices for orders that were subject to display price sliding.

C. *Latency*

Latency is the time it takes to accept and process orders on an exchange and then to send back the resulting acknowledgment to the customer. A system's latency is affected by a variety of sources, including hardware processing capabilities, cabling, network equipment, and the manner in which the hardware components are paired with the software.

Petitioner offered customers ultralow latency through its trading system, allowing customers to quickly place, modify, or cancel orders on the Exchanges. Low latency gives customers greater control over their orders and allows them to respond more rapidly to changing market conditions and mitigate trade execution risk. The low latency petitioner offered was important to many of its customers, particularly to those that were market makers. Petitioner achieved low latency through both its software and its hardware.

D. *SEC Form 19b–4 Filings*

The securities laws required petitioner to file copies of any proposed changes to its Exchange Rules with the SEC, accompanied by an explanation of the basis and purpose of the proposed changes. *See* 15 U.S.C. § 78s(b)(1). Petitioner filed multiple Forms 19b–4 during the years in issue to submit these proposed rule changes.

On its Forms 19b–4 petitioner described the logical port fees as fees for logical ports, which petitioner stated were "commonly referred to as TCP/IP port[s]." Petitioner also referred to the logical port fees as fees for connectivity. The routing fees were described as fees for executions of orders routed to external markets using petitioner's routing services. The transaction fees were described as fees for executions that removed liquidity from the BZX order book or added liquidity to the BYX order book. Petitioner did not use the word "software" to describe the Fees.

VI. *Commercially Available Trading Software*

During the years in issue multiple vendors (collectively, third-party vendors) made customizable electronic trading platforms commercially available to customers. Cinnober Financial Technology AB (Cinnober) offered the TRADExpress Trading System; NYSE Technologies, Inc. (NYSE Technologies), a subsidiary of NYSE Euronext, offered the Universal Trading Platform (UTP); and Millennium Information Technologies (Pvt) Ltd. (MillenniumIT) offered the Millennium Exchange.

To operate an electronic market as a business using the commercially available trading platforms, customers receiving such platforms from the third-party vendors needed to launch their own electronic market, comply with any relevant regulatory requirements, admit members to be eligible to transact on the electronic market, and establish connectivity with users so they could submit orders to the market and receive order status updates and market data. The third-party vendors' customers were able to set or change user permissions and to determine who would be able to submit orders to their markets.

The third-party vendors offered customers licenses of their trading software, whereby they installed their trading software onto customers' hardware. MillenniumIT's customers received the Millennium Exchange software on their own servers at their respective data centers, pursuant to a Licensing and Maintenance Agreement, and also received that software affixed to a tangible medium. NYSE Euronext offered licenses of UTP whereby the UTP software would be installed on the customer's hardware. Cinnober offered its TRADExpress Trading System to customers pursuant to a software license agreement. Cinnober and NYSE Technologies also offered "hosted" arrangements, whereby they installed the TRADExpress Trading System software and the UTP software, respectively, onto their own hardware and managed the system on behalf of their customers. Customers of Cinnober and NYSE Technologies did not receive rights to make copies of the trading software.

VII. *Intuit Inc.'s TurboTax Software*

Intuit Consumer Group, Inc., was a subsidiary of Intuit Inc. during the years in issue. Intuit Consumer Group, Inc. (Intuit), offered customers TurboTax tax return preparation software (TurboTax) on CD, by download over the internet, and for use online over the internet. Intuit had a business model of providing TurboTax software for a fee so that customers could prepare their own tax returns.

The online use of TurboTax was described in Intuit's Forms 10–K for the years in issue as "hosted services" or "software as a service." During the years in issue customers using TurboTax software online agreed to a terms of service agreement, which incorporated by reference product and payment terms from TurboTax's website. Customers were unable to modify the software, change where it ran, configure it, or exercise administrator privileges such as installing or removing the software.

VIII. *Federal Tax Returns*

On its originally filed federal income tax returns petitioner claimed deductions under section 199 of $2,644,895, $3,769,767, and $4,074,241 for 2011, 2012, and 2013, respectively. Petitioner attached to its returns Forms 8903, Domestic Production Activities Deduction, and reported DPGR of $683,205,964, $593,695,917, and $571,054,106 for 2011, 2012, and 2013, respectively. Petitioner initially included in its reported DPGR the gross receipts from certain physical port fees and logical port fees for market data ports. Petitioner has since conceded that these amounts were not allowable as DPGR and has revised its claimed DPGR to $677,131,949, $584,942,070, and $559,317,821 for 2011, 2012, and 2013, respectively.

OPINION

We must decide whether petitioner's gross receipts from the Fees are DPGR. To be DPGR the Fees must satisfy the requirements of Treasury Regulation § 1.199-3(i)(6)(iii)(B): first, that they were derived from providing customers access to computer software for the customers' direct use while connected to the internet or any other public or private communications network, *id.* subdiv. (iii); and second, that a third party derived gross receipts from the lease, rental, license, sale, exchange, or other disposition of substantially identical software, *id.* subdiv. (iii)(B). The parties dispute whether petitioner met the threshold requirements of subdivision (iii) and whether petitioner met the further requirements of subdivision (iii)(B).

Respondent determined that none of petitioner's gross receipts from the Fees were DPGR. Generally, the Commissioner's determinations are presumed correct, and the taxpayer bears the burden of proving the Commissioner's determinations are erroneous. Rule 142(a); *Welch v. Helvering*, 290 U.S. 111, 115 (1933). The burden of proof may shift to the Commissioner if the taxpayer establishes that he or she complied with the requirements of section 7491(a) to substantiate items, to maintain required records, and to cooperate fully with the Commissioner's reasonable requests. The record allows us to decide this case without regard to which party bears the burden of proof. *See Gibson & Assocs., Inc. v. Commissioner*, 136 T.C. 195, 221 (2011).

I. *Section 199 Deduction*

Congress enacted section 199 as part of the American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 102(a), 118 Stat. 1418, 1424, to provide a tax deduction for certain domestic production activities. Section 199 was intended to stimulate job creation in the United States and strengthen the economy by reducing the tax burden on domestic manufacturers. *See ADVO, Inc. & Subs. v. Commissioner*, 141 T.C. 298, 311–12 (2013) (citing *Gibson & Assocs., Inc.*, 136 T.C. at 223). Section 199 was repealed for tax years beginning after December 31, 2017. Tax Cuts and Jobs Act of 2017, Pub. L. No. 115-97, § 13305(a), (c), 131 Stat. 2054, 2126.

As in effect during the years in issue, section 199(a) allows a deduction equal to 9% of the lesser of (1) the qualified production activities income (QPAI) of the taxpayer for the tax year, or (2) taxable income (determined without regard to section 199) for the tax year. The amount of the deduction is limited to 50% of the wages of the taxpayer reported on Form W–2, Wage and Tax Statement, for the taxable year that are properly allocable to DPGR. § 199(b). QPAI for any taxable year is an amount equal to the excess, if any, of (A) the taxpayer's DPGR for such taxable year, over (B) the sum of (i) the cost of goods sold allocable to such receipts and (ii) other expenses, losses, or deductions (other than the deduction under section 199) that are properly allocable to such receipts. § 199(c)(1).

DPGR includes gross receipts derived from any lease, rental, license, sale, exchange, or other disposition of qualifying production property (QPP) that was manufactured, produced, grown, or extracted (MPGE) by the taxpayer in whole or in significant part within the United States. § 199(c)(4)(A)(i)(I). The regulations specify that the term "derived from the lease, rental, license, sale, exchange, or other disposition" (collectively, disposition) is limited to the gross receipts directly derived from the disposition of QPP and note that applicable federal income tax principles apply to determine whether a transaction is a lease, rental, license, sale, exchange or other disposition, a service, or some combination thereof. Treas. Reg. § 1.199-3(i)(1)(i).

QPP includes any computer software. § 199(c)(5)(B). The regulations define computer software as "any program or routine or any sequence of machine-readable code that is designed to cause a computer to perform a desired function or set of functions, and the documentation required to describe and maintain that program or routine." Treas. Reg. § 1.199-3(j)(3)(i).

The definition of DPGR specifically does not include gross receipts derived from services; however, there is an exception for gross receipts derived from engineering or architectural services performed in the United States. § 199(c)(4)(A)(iii). Gross receipts from construction performed in the United States are also included. § 199(c)(4)(A)(ii). The regulations clarify that except as otherwise provided, gross receipts derived from the performance of services do not qualify as

DPGR. Treas. Reg. § 1.199-3(i)(4)(i)(A). In the case of an embedded service, that is, a service for which the price, in the normal course of the taxpayer's business, is not separately stated from the amount charged for the lease, rental, license, sale, exchange, or other disposition of QPP, DPGR includes only the gross receipts derived from the disposition of QPP and not any receipts attributable to the embedded service. *Id.*

A. *Computer Software*

DPGR includes gross receipts derived from the lease, rental, license, sale, exchange, or other disposition of computer software MPGE by the taxpayer in whole or in significant part within the United States. *Id.* subpara. (6)(i). Such gross receipts qualify as DPGR even if the customer provides the computer software to its employees or others over the internet. *Id.* Consistent with the general treatment of services under section 199, gross receipts derived from customer and technical support, telephone and other telecommunication services, online services (such as internet access services, online banking services, providing access to online electronic books, newspapers, and journals), and other similar services do not constitute gross receipts derived from a lease, rental, license, sale, exchange, or other disposition of computer software. Treas. Reg. § 1.199-3(i)(6)(ii).

The regulations provide narrow exceptions to the general rule excluding online services from DPGR. Notwithstanding Treasury Regulation § 1.199-3(i)(6)(ii), if a taxpayer derives gross receipts from providing customers access to computer software MPGE in whole or in significant part by the taxpayer within the United States for the customers' direct use while connected to the internet or any other public or private communications network (online software), such gross receipts will be treated as derived from the disposition of computer software only if Treasury Regulation § 1.199-3(i)(6)(iii)(A) or (B) is met. *Id.* subdiv. (iii).

Treasury Regulation § 1.199-3(i)(6)(iii)(A) requires that the taxpayer also derive, on a regular and ongoing basis in the taxpayer's business, gross receipts from the disposition to customers of computer software that has only minor or immaterial differences from the online software in a tangible medium or by download. We refer to subdivision (iii)(A) as the self-comparable exception. *Cf., e.g.*, I.R.S. Chief Couns. Adv. Mem. 201603028 (Jan. 15, 2016). Petitioner does not assert that it meets the requirements of the self-comparable exception.

Treasury Regulation § 1.199-3(i)(6)(iii)(B) requires that another person derive, on a regular and ongoing basis in its business, gross receipts from the disposition in a tangible medium or by download of substantially identical software (as compared to the taxpayer's online software) to its customers. We refer to subdivision (iii)(B) as the third-party comparable exception. *Cf., e.g.*, I.R.S. Chief Couns. Adv. Mem. 201603028. For purposes of the third-party comparable exception substantially identical software is computer software that (1) from a customer's perspective has the same functional result as the taxpayer's online software and (2) has a significant overlap of features or purpose with the taxpayer's online software. Treas. Reg. § 1.199-3(i)(6)(iv)(A).

B. *Background on the Exceptions*

On January 19, 2005, the Department of the Treasury (Treasury) issued I.R.S. Notice 2005-14, 2005-1 C.B. 498, to provide interim guidance on section 199. The notice stated: "Except as provided in the safe harbor [for embedded services], gross receipts derived by a taxpayer from software that is merely offered for use to customers online for a fee are not DPGR." *Id.*, 2005-1 C.B. at 508. This general rule, that the provision of online software constituted a service, was also reflected in the proposed regulations published November 4, 2005, which stated that "the use of online computer software does not rise to the level of a lease, rental, license, sale, exchange, or other disposition as required under section 199 but is instead a service." REG-105847-05, 70 Fed. Reg. 67,220, 67,226; *see also id.* at 67,250. Treasury requested comments "concerning whether gross receipts derived from the provision of certain types of online software should qualify under section 199 as being derived from a lease, rental, license, sale, exchange, or other disposition of the software and, if so, how to distinguish between such types of online software." *Id.* at 67,239.

On June 12, 2006, Treasury issued temporary regulations regarding section 199. The supplementary information to the temporary regulations noted that on July 21, 2005, the Chairman and the Ranking Member of the Senate Finance Committee and the Chairman of the House Ways and Means Committee sent a letter to Treasury regarding the treatment of online access to computer software. T.D. 9262, 2006-1 C.B. 1040, 1040–41. The letter requested that Treasury consider whether the treatment of computer software accessed online should be similar to the treatment of computer software distributed by other means, such as by physical delivery or delivery via internet download. *Id.*, 2006-1 C.B. at 1041. The letter also noted that "gross receipts from the provision of services are not treated as DPGR, regardless of the fact that computer software may be used to facilitate such service transactions." *Id.*

The supplementary information to the temporary regulations also summarized comments regarding the treatment of online software. Comments suggested that a customer's use of computer software is tantamount to a license of the computer software. *Id.* Other commentators suggested that "other disposition" in section 199(c)(4)(A) is broad enough to include the provision of computer software for online use. *Id.* These comments were not incorporated into the temporary regulations. *Id.* Instead, the temporary regulations introduced two exceptions to the overall exclusion of gross receipts derived from online software from DPGR.

The supplementary information noted that these exceptions, the self-comparable exception and the third-party comparable exception, were added "as a matter of administrative convenience" to provide "two exceptions under which gross receipts derived by a taxpayer from providing computer software to customers for the customers' direct use while connected to the Internet will be treated as being derived from the lease, rental, license, sale, exchange, or other disposition of such computer software." *Id.*

On April 16, 2007, Treasury promulgated final regulations under section 199. The supplementary information to the final regulations reiterates first the general rule that gross receipts derived from online services are excluded from DPGR, and second, the two exceptions from this rule, under which gross receipts derived from online software are treated as DPGR. T.D. 9317, 2007-1 C.B. 957, 958.

II. *Fees*

In order for the Fees to be treated as DPGR, the requirements of Treasury Regulation § 1.199-3(i)(6)(iii) must be met. Petitioner must first show that the Fees were derived from providing customers access to computer software MPGE in whole or in significant part by petitioner within the United States for customers' direct use while connected to the internet or any other public or private communications network. *See id.* If this first requirement is met, petitioner must show that either the self-comparable exception or the third-party comparable exception is met. *See id.*

Petitioner contends that it made a disposition of computer software for its customers' direct use. We disagree. Petitioner did not provide its customers direct access to its software as defined in the Code and the regulations.

A. *Logical Port Fees*

Petitioner claimed its logical port fees as DPGR because it contends that the logical port fees were derived from providing customers access to the order handler component of its trading software for the customers' direct use.[1] Access to logical ports provided customers with access to petitioner's private communications network. In other words, the logical ports provided connectivity.

The logical ports validated customers' orders and forwarded them to the matching engine. Petitioner charged the logical port fees at a flat monthly rate for each FIX or BOE port assigned to a customer. The fee for each logical port did not increase or decrease according to whether a customer submitted, modified, or canceled orders.

Logical ports enabled customers to interact with the Exchanges. The connection through the logical ports took the place of going to an exchange in person. This interaction is similar to internet access services that enable users to browse the world wide web, to transfer files, and to access email. *See Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 987 (2005). Gross receipts from internet access services do not constitute gross receipts derived from a lease,

[1] After concessions, the only logical port fees petitioner claims as DPGR are those charged for logical connectivity to petitioner's system.

rental, license, sale, exchange, or other disposition of software. *See* Treas. Reg. § 1.199-3(i)(6)(ii). Connection to the logical ports is akin to internet access rather than direct use as described in Treasury Regulation § 1.199-3(i)(6)(iii)(B).

The logical port fees are payments for access to petitioner's private communications network. Accordingly, the logical port fees are not DPGR. The applicable regulations provide examples that contrast what is DPGR and is not DPGR. Example 3 addresses N, a provider of telephone services, voicemail services, and email services. Treas. Reg. § 1.199-3(i)(6)(v) (example 3). N produces computer software in the United States that runs the above-described services. *Id.* This example concludes that N's gross receipts derived from the telephone and other communication services are non-DPGR because Treasury Regulation § 1.199-3(i)(6)(ii) excludes gross receipts derived from telephone and related communication services from gross receipts derived from a disposition of computer software. *Id.* Petitioner's logical port fees are analogous to Example 3. Both fees are for services that provide the customer with a connection.

B. *Routing Fees*

Petitioner claimed its routing fees as DPGR. Petitioner contends that the routing fees were derived from providing customers access to the routing-related functionality of its trading software for the customers' direct use.

The routing fees were charged only upon the execution of a customer's order on an external market. Customers could select different routing strategies for how their orders would be routed to different markets. The price of the fee per share or option contract executed varied with the strategy the customer selected.

Pursuant to petitioner's securities routing agreement, BATS Trading, Inc., routed orders to external exchanges as the customers' agent. Sometimes a third party, such as Morgan Stanley, routed customers' orders on behalf of BATS Trading, Inc. In routing customers' orders, BATS Trading, Inc., paid transaction, connectivity, and membership fees charged by the external exchanges. Petitioner asserts that the involvement of BATS Trading, Inc., in routing customers' orders was a legal formality because of the applicable regulatory scheme.

Petitioner further asserts that customers should really be considered to route their own orders.

Customers did not use petitioner's software to route their orders. They could only submit orders with instructions as to routing strategy. BATS Trading, Inc., pursuant to the securities routing agreement, acted as the customers' agent for the purpose of providing these routing services. The varying prices customers paid for routing strategies reflected the different services petitioner provided, such as routing orders to particular types of external markets. Customers paid for different services, not different uses of the trading software.

The routing fees were charged for the routing and trade execution services performed for customers. They were not derived from customers' access to software for their direct use.

C. *Transaction Fees*

Petitioner claimed its transaction fees as DPGR. Petitioner contends that the transaction fees were derived from providing customers access to the matching-related functionality of its trading software for the customers' direct use.

The transaction fees were charged only upon the execution of a customer's order. A customer's trade could not be executed solely by the customer's submitting a bid or offer to the Exchanges; trade executions required counterparties. The rebates petitioner offered, which on average were equal to 79% of the transaction fees petitioner received, were a core part of petitioner's business strategy to attract those counterparties to the Exchanges.

Petitioner's transaction fees were not charged to customers according to the extent to which they made use of the Exchanges. Not every submitted order was executed, and therefore not every submitted order triggered a transaction fee. Not every customer whose order was executed paid a transaction fee, because one party to each trade was issued a rebate. A customer who was charged a fee took the same actions to submit an order as the customer who was issued a rebate or the customer whose submitted order was never executed. The transaction fees were charged to customers according to how much they accessed or removed liquidity, depending on the relevant exchange, as reflected in petitioner's fee schedules, where the transaction fees were referred to as "Fees for Accessing Liquidity" or "Liquidity Fees." They thus reflected the trade execution services petitioner provided.

The varying prices petitioner charged customers for different order types also demonstrate that the transaction fees were derived from services. The different prices of the transaction fees reflected the different services petitioner performed for customers, such as hiding their orders from being displayed in market data or adjusting the order prices using display price sliding. Customers paid for different services, not different uses of the trading software.

The regulations provide an analogous example of a company that uses computer software to provide online services to customers. Example 2 describes M, an internet auction company that produces computer software within the United States that enables its customers to participate in internet auctions for a fee. Treas. Reg. § 1.199-3(i)(6)(v) (example 2). The example does not elaborate on how M's auction software enabled customers to participate in internet auctions or how M's customers participated in internet auctions; it focuses only on the fact that M's activities constituted the provision of online services. The example concludes that M's gross receipts derived from the internet auction services are non-DPGR because Treasury Regulation § 1.199-3(i)(6)(ii) excludes gross receipts derived from online services from gross receipts derived from a disposition of computer software.

Petitioner's transaction fees are analogous to Example 2. Both petitioner and M, the company in the example, charged their customers fees for participation in electronic markets and facilitated this service with computer software. Petitioner's provision of trade execution services was an online service within the meaning of Treasury Regulation § 1.199-3(i)(6)(ii). Petitioner's customers did not directly use its software within the meaning of Treasury Regulation § 1.199-3(i)(6)(iii).

D. *Conclusion to the Fees*

Petitioner is an operator of securities exchanges. The fact that the Exchanges use software to operate does not convert petitioner's trade execution services into the provision of software for customers' direct use.

Petitioner further contends that the regulatory requirements of access and direct use should be interpreted with reference to TurboTax, Intuit's online tax preparation software. Petitioner points to regulatory examples showing that providing customers access to online tax preparation software constitutes access and direct use for purposes of the regulation. *See* Treas. Reg. § 1.199-3(i)(6)(v) (examples 4 and 5). Examples 4 and 5 illustrate the self-comparable exception and the third-party comparable exception, respectively, using the example of a company that derives gross receipts from providing customers access to online tax preparation software for customers' direct use while connected to the internet. *Id.* Petitioner argues that the way Intuit's customers interacted with TurboTax was not meaningfully different from how its customers interacted with the trading software. We disagree with petitioner that its trading software can be compared to TurboTax.

The developers of tax preparation software have a business model that consists of supplying online software for a fee so customers can prepare their tax returns. Petitioner, in contrast, used its trading software as part of its business to provide services to its customers. Unlike the tax preparation company in the examples, petitioner did not offer customers its trading software on CD or by download over the internet, nor has it shown that third parties offered customers substantially identical software to its trading software. Petitioner is more like the companies described in regulatory Examples 1 and 2, which produce computer software that they use as part of their business. *See id.* (examples 1 and 2). In Example 1, a bank produces computer software that enables its customers to receive online services for a fee. In Example 2, an internet auction company produces computer software that enables its customers to participate in internet auctions for a fee. Petitioner and Intuit used their software in different ways in their respective businesses and are not comparable.

Petitioner's customers could submit orders to the Exchanges, but they could not themselves use the trading software to route or execute their orders. They could only request that petitioner perform these trade execution services. Petitioner's agreements with its customers show that customers received services, not the use of software, from petitioner. The user agreement characterized customers' access to the Exchanges for order entry and trade execution as services, not as the direct use of software. Likewise, the securities routing agreement referred to routing services, to be performed by BATS Trading, Inc.

Petitioner repeatedly characterized its Fees as fees for providing trade execution services to customers, not fees for the direct use of software. Further, petitioner's filings with the SEC did not describe the Fees as fees for customer use of software. Instead, petitioner represented that the logical port fees were for connectivity to its Exchanges, that the routing fees were for the execution of orders routed to external markets using petitioner's routing services, and that the transaction fees were for adding or removing liquidity. Petitioner also represented to the SEC that the Exchanges, not customers, were responsible for matching and executing orders. *See* 17 C.F.R. § 240.3b-16(a)(1). Consistent with petitioner's representations, the Fees were derived from services, not the direct use of software. *See* Treas. Reg. § 1.199-3(i)(6)(iii).

III. *Third-Party Comparable Exception*

We hold that petitioner did not meet the threshold requirements of Treasury Regulation § 1.199-3(i)(6)(iii) with respect to the Fees. In the alternative, we consider whether petitioner met the further requirements of one of the exceptions under subdivision (iii), the self-comparable exception or the third-party comparable exception. In this case petitioner argues only that it meets the requirements of the third-party comparable exception, Treasury Regulation § 1.199-3(i)(6)(iii)(B). Petitioner does not meet those requirements.

For petitioner to qualify for the third-party comparable exception, a third party must derive, on a regular and ongoing basis in its business, gross receipts from the disposition to its customers of software that is substantially identical to petitioner's online software in a tangible medium or by download. *See id.* In order to be substantially identical to petitioner's software for purposes of Treasury Regulation § 1.199-3(i)(6)(iii)(B), a third-party vendor's computer software must (1) from a customer's perspective, have the same functional result as petitioner's online software and (2) have a significant overlap of features or purpose with petitioner's online software. *See id.* subdiv. (iv)(A).

Petitioner contends that respondent's interpretation of the substantially identical requirement is too narrow. It disputes respondent's position that for software to be substantially identical, the user of the taxpayer's software and the immediate purchaser of the third party's software must use the respective software in the same way. Petitioner's position is that only the software itself needs to be comparable.

The plain meaning of a regulation governs if the regulation is not ambiguous. *Safe Air For Everyone v. EPA*, 488 F.3d 1088, 1097 (9th Cir. 2007). A court must consider the text, structure, history, and purpose of a regulation before concluding that it is genuinely ambiguous. *Kisor v. Wilkie*, 139 S. Ct. 2400, 2415 (2019); *see also Amazon.com, Inc. & Subs. v. Commissioner*, 934 F.3d 976, 984 (9th Cir. 2019), *aff'g* 148 T.C. 108 (2017).

Treasury regulations must be interpreted in the context of the statute they are designed to explicate. *Bank of New York v. United States*, 526 F.2d 1012, 1018 (3d Cir. 1975). Regulations are not an opportunity to amend a statute. *United States v. Calamaro*, 354 U.S. 351, 359 (1957); *Koshland v. Helvering*, 298 U.S. 441, 447 (1936). Petitioner's interpretation of Treasury Regulation § 1.199-3(i)(6)(iii) would expand the definition of DPGR to include gross receipts derived from services as long as online software facilitated or enabled those services.

For its expansive view of the regulation petitioner relies upon the safe harbor for computer software games found in Treasury Regulation § 1.199-3(i)(6)(iv)(B). The safe harbor provides that all computer software games are deemed to be substantially identical for purposes of Treasury Regulation § 1.199-3(i)(6)(iv)(A), which describes the substantially identical software requirement of the third-party comparable exception. Petitioner contends the definition of substantially identical software is broad and consistent with the safe harbor for computer software games. It argues that the safe harbor treats all games as substantially identical even though there are significant differences among games. Petitioner points out that the safe harbor explains that computer software sports games are deemed substantially identical to computer software card games. *See id.* subdiv. (iv)(B).

We disagree with petitioner that the safe harbor supports a broad interpretation of substantially identical software. The safe harbor is unambiguous. The safe harbor is titled "Safe harbor for computer software games." It states "all computer software games," which clearly does not include other types of software, such as trading software. *See id.*

Treating all computer games as substantially identical software clearly does not mean that other types of software, such as trading software, can be treated as substantially identical software. This Court has traditionally taken the position that our responsibility is to apply the law to the facts of the case before us and not look at how other taxpayers have been treated. *Gaughf Props., L.P. v. Commissioner*, 139 T.C. 219, 254 (2012) (citing *Davis v. Commissioner*, 65 T.C. 1014, 1022 (1976)), *aff'd*, 738 F.3d 415 (D.C. Cir. 2013). If all trading software is to be treated as substantially identical software, it should have been included in the safe harbor or the regulation should have provided an additional safe harbor for it. As written, the safe harbor applies only to computer games and has no implications for whether a third-party vendor's trading software would qualify as substantially identical software.

Respondent's application of Treasury Regulation § 1.199-3(i)(6)(iv)(A) is not arbitrary simply because it results in different treatment for different taxpayers. In matters of taxation the selection of subjects of taxation, rates, classes of beneficiaries, and permissible deductions has a large element of arbitrariness. *Danly Mach. Corp. v. United States*, 492 F.2d 30, 33 (7th Cir. 1974). Congress may give a deduction to all in a narrowly defined class and deny it to those who are distinguishable from the class. *Id.* The safe harbor unambiguously applies only to computer software games, and respondent reasonably interprets the definition of substantially identical software without reference to the safe harbor.

Petitioner further contends that the requirement that substantially identical software have the same functional result from a customer's perspective does not demand comparability between the taxpayer's customers and customers of a third party. It argues that the "customer" referred to in the regulation should be understood to include not just the customers from whom the third-party vendors derived gross receipts, but also the customers of those customers. Petitioner would include as customers the entities that traded on the exchanges run by the third-party vendor's customers. Respondent contends that a "customer" refers to the third-party vendors' actual customers, which in this case would be the exchange operators.

We interpret a regulation in the context of the regulatory scheme as a whole. *McCarthy v. Bronson*, 500 U.S. 136, 139 (1991). Treasury Regulation § 1.199-3(i)(6)(iii)(B) specifically uses the words "to its customers" and this clearly means the customers of the third-party vendor. The "substantially identical software" definition in Treasury Regulation § 1.199-3(i)(6)(iv)(A) uses the words "a customer's perspective." Respondent contends this wording means a customer of the third party that provides the comparable software for purposes of the third-party comparable exception.

We agree with respondent's interpretation. Petitioner's interpretation ignores the context of the definition of substantially identical software. The definition is provided specifically for purposes of Treasury Regulation § 1.199-3(i)(6)(iii)(B). *See id.* subdiv. (iv)(A). The definition, and its reference to a "customer," cannot be considered without looking at Treasury Regulation § 1.199-3(i)(6)(iii)(B). The two subdivisions, read together, require that the functional result of a third-party vendor's software be evaluated from the perspective of an actual customer receiving the commercially available trading software from the third-party vendor, as compared with the perspective of petitioner's customers.

Petitioner argues that it meets this requirement through the commercially available trading software of the third-party vendors: NYSE Euronext, which offered the UTP; Cinnober, which offered the TRADExpress Trading System; and MillenniumIT, which offered the Millennium Exchange. Customers of the third-party vendors received the commercially available trading software on their own hardware, pursuant to license agreements. They could then use the software to operate electronic markets.

Petitioner's trading software was also used to operate electronic markets during the years in issue. However, petitioner itself operated the Exchanges. Petitioner's customers could only submit, cancel, and modify orders to trade securities. Petitioner's customers did not execute license agreements with petitioner and could not operate their own electronic markets using petitioner's Exchanges.

Trading securities and operating a securities exchange are two distinct activities and are not the same functional result from a customer's perspective. Petitioner and the third-party vendors had fundamentally different relationships with their customers with regard to the operation of a securities exchange. For the third-party vendors, there were three steps in the relationship: first, the third-party vendors developed trading software that they licensed to customers; second, customers used the software to run their own exchanges; and third, members of the exchanges (whether the operators of the exchanges or their own customers) participated in trading on the exchanges. Petitioner, on the other hand, skipped this middle step and offered its customers participation in trading on its exchanges.

The regulatory examples, although they do not provide a definition of "functional result" or "features or purpose," are instructive. In Examples 5 and 6, a third party that provides customers access to a particular type of computer software is stated to offer substantially identical software to a taxpayer that provides customers with the same type of computer software. Treas. Reg. § 1.199-3(i)(6)(v) (examples 5 and 6). The Examples therefore show that a third party's computer software that its customers use for a particular activity (tax preparation, in Example 5, or payroll management, in Example 6) can be substantially identical software as compared to a taxpayer's computer software that is used for the same activity.

In Example 7, a third party's payroll management software is stated not to be substantially identical software as compared to the taxpayer's inventory computer software. *Id.* (example 7). The extent of the detail that the Example provides about the two companies is that the taxpayer company's customers use its software for inventory, and the third party's customers use its software to manage payrolls. These are two distinct activities.

The third-party vendors' software is not substantially identical to petitioner's software within the meaning of Treasury Regulation § 1.199-3(i)(6)(iv)(A), and therefore petitioner does not meet the requirements of the third-party comparable exception. *See id.* subdiv. (iii)(B).

IV. *Conclusion*

Petitioner claimed the gross receipts from its Fees as DPGR. All three categories of Fees at issue—transaction fees, routing fees, and logical port fees—were derived from services petitioner performed for customers in the course of operating its Exchanges. The Fees were not derived from providing customers access to computer software for their direct use, and they therefore do not meet the requirements of Treasury Regulation § 1.199-3(i)(6)(iii).

Even if the Fees could meet the requirements of Treasury Regulation § 1.199-3(i)(6)(iii), they do not meet the further requirements of the third-party comparable exception. Petitioner has not demonstrated that a third party derived gross receipts from the disposition to its customers of software that was substantially identical to petitioner's online software. *See id.* subdiv. (iii)(B).

Any contentions we have not addressed are irrelevant, moot, or meritless.

To reflect the foregoing,

Decision will be entered under Rule 155.

TREECE FINANCIAL SERVICES GROUP, PETITIONER *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 20850-19. Filed April 19, 2022.

P, a corporation, petitioned for review of a notice of employment tax determination under I.R.C. § 7436. The parties agree that respondent properly determined that E is an employee of P but dispute the proper amount of employment tax under that determination. P asserts that the amount should be computed using R's Announcement 2012-45, 2012-51 I.R.B. 724, entitled Voluntary Classification Settlement Program (VCSP). R determined that P may not use the VCSP to compute the proper amount of employment tax and argues that the Court lacks jurisdiction to review that determination. R moved to partially dismiss for lack of jurisdiction. P moved for summary

judgment. *Held*: R's motion will be denied. The Tax Court has jurisdiction in this employment tax case to determine whether R's determination that the VCSP does not apply to the computation of P's employment tax liability is correct. *Held*, *further*, P's motion will be denied. There remains a genuine dispute of material fact as to whether the VCSP applies here.

Mark M. Mockensturm and *Blanca N. Wheeler*, for petitioner.
Gabriel J. Minc, for respondent.

OPINION

KERRIGAN, *Judge*: This case is before the Court on respondent's Motion to Partially Dismiss for Lack of Jurisdiction and petitioner's Motion for Summary Judgment. Respondent contends that this Court lacks jurisdiction in this employment tax case to review respondent's determination that the Voluntary Classification Settlement Program (VCSP) does not apply to the computation of petitioner's employment tax liabilities. Petitioner contends that it met all the requirements of the VCSP and respondent does not have the discretion to deny its participation in the VCSP.

Unless otherwise indicated, all statutory references are to the Internal Revenue Code, Title 26 U.S.C., in effect at all relevant times, and all Rule references are to the Tax Court Rules of Practice and Procedure. All monetary amounts are rounded to the nearest dollar.

On October 10, 2019, respondent sent Treece Financial Services Group a Letter 3523, Notice of Employment Tax Determination Under IRC 7436 (notice), reclassifying Dock D. Treece as an employee instead of an independent contractor for tax years 2015, 2016, and 2017 (years in issue). In the notice respondent determined additions to tax pursuant to section 6651(a) and penalties pursuant to section 6656 for the years in issue. On September 13, 2021, the parties filed a Stipulation of Settled Issues which resolved all but one issue. The remaining issue is the proper amounts of employment taxes which petitioner seeks to have computed in accordance with respondent's VCSP.

The parties stipulated that Mr. Treece was the sole corporate officer of petitioner for the years in issue. They further stipulated that he was an employee and not an independent contractor for the years in issue. The parties also stipulated that petitioner is not entitled to relief under the Revenue Act of 1978, Pub. L. No. 95-600, § 530, 92 Stat. 2763, 2885, as amended, with respect to Mr. Treece's treatment as an independent contractor.

Pursuant to the Stipulation of Settled Issues petitioner owes the following employment taxes:

Tax period	*Return form number*	*Type of tax*	*Amount of tax*
3/31/15–12/31/15	941	FICA & FITW	$3,738
2015	940	FUTA	420
3/31/16–12/31/16	941	FICA & FITW	4,988
2016	940	FUTA	420
3/31/17–12/31/17	941	FICA & FITW	8,576
2017	940	FUTA	420
Total			**$18,562**

These amounts are subject to reduction if petitioner qualifies for the VCSP.

Respondent abated additions to tax pursuant to section 6651(a) and penalties pursuant to section 6656.

Background

There is no dispute as to the following facts drawn from the parties' motion papers, affidavits, and attached exhibits. When the Petition was timely filed, petitioner was a corporation with its principal place of business in Ohio. Mr. Treece is a principal of petitioner.

The VCSP provides partial relief from federal employment taxes for eligible taxpayers that agree to treat workers prospectively as employees. I.R.S. Announcement 2012-45, 2012-51 I.R.B. 724, 724. To be eligible for the VCSP, a taxpayer must (1) have consistently treated the workers as nonemployees; (2) have filed all required Forms 1099, consistent with the nonemployee treatment, for the previous three years; and (3) not currently be under employment tax audit by the Internal Revenue Service (IRS). *Id.* Petitioner submitted Form 8952, Application for Voluntary Classification Settlement Program (VCSP), on October 23, 2018. Respondent denied petitioner participation in the VCSP on February 28, 2019, stating: "You're under an employment tax examination by the IRS."

Discussion

We will first decide respondent's Motion to Partially Dismiss. If we determine that we have jurisdiction, we will then address petitioner's Motion for Summary Judgment.

I. *Respondent's Motion to Partially Dismiss*

The Tax Court may exercise jurisdiction only to the extent expressly provided by Congress. *See* § 7442; *Breman v. Commissioner*, 66 T.C. 61, 66 (1976). We, however, have the authority to determine whether we have jurisdiction over a particular case. *Kluger v. Commissioner*, 83 T.C. 309, 314 (1984). Generally, we have jurisdiction under section 7436(a) to determine (1) whether an individual providing services to a person is that person's employee for purposes of subtitle C; (2) whether the person, if an employer, is entitled to relief under section 530 of the Revenue Act of 1978; and (3) the proper amounts of employment taxes which relate to the Commissioner's determination concerning worker classification.

This Court's deficiency jurisdiction includes reviewing administrative determinations that are necessary to determine the merits of the deficiency determinations. *See, e.g., Trimmer v. Commissioner*, 148 T.C. 334, 345–48 (2017) (holding that the Tax Court has jurisdiction in a deficiency proceeding to review the Commissioner's denial of the taxpayer's request for a hardship waiver of the 60-day rollover requirement under section 402(c)(3)(B)); *Capitol Fed. Sav. & Loan Ass'n & Sub. v. Commissioner*, 96 T.C. 204, 214–15 (1991) (holding that the Commissioner's refusal to process an application for an accounting method change under section 446(b) is subject to judicial review in a deficiency proceeding); *Mailman v. Commissioner*, 91 T.C. 1079, 1083 (1988) (holding that the Commissioner's denial of waiver of the addition to tax under former section 6661 is subject to judicial review in a deficiency proceeding); *Estate of Gardner v. Commissioner*, 82 T.C. 989, 1000 (1984) (holding that the Commissioner's denial of a request under section 6081(a) to extend the time for filing of an estate tax return is subject to judicial review in a deficiency proceeding). Under section 7436(d), the principles of sections

6213(a), (b), (c), (d), and (f), 6214(a), 6215, 6503(a), 6512, and 7481 apply to cases that arise under section 7436, as if the Secretary's notice of determination was a notice of deficiency. *Charlotte's Office Boutique, Inc. v. Commissioner*, 121 T.C. 89, 103 n.8 (2003), *supplemented by* T.C. Memo. 2004-43, *aff'd,* 425 F.3d 1203 (9th Cir. 2005).

There is a strong presumption that an act of administrative discretion is subject to judicial review. *Trimmer*, 148 T.C. at 346; *Corbalis v. Commissioner*, 142 T.C. 46, 56 (2014) (holding that denials of interest suspension under section 6404(h) are subject to judicial review). Under the VCSP, an eligible employer pays a lesser amount of employment tax than would have been due as to certain employees and is not liable for any interest and penalties. *See* I.R.S. Announcement 2012-45, 2012-51 I.R.B. at 725. In 2000 section 7436(a) was amended to provide the Tax Court jurisdiction to "determine whether such a determination by the Secretary is correct and the proper amount of employment tax under such determination." *See* Consolidated Appropriations Act, 2001, Pub. L. No. 106-554, § 314(f), 114 Stat. 2763, 2763A-643 (2000); Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, § 3103, 112 Stat. 685, 731. The U.S. Court of Appeals for the Ninth Circuit held that the amendment in 2000 "indicates that Congress did not intend to limit the Tax Court's jurisdiction under section 7436 to determining only whether an individual was an employee." *Charlotte's Office Boutique, Inc. v. Commissioner*, 425 F.3d at 1208.

Pursuant to statute and caselaw we conclude that this Court has jurisdiction to determine whether the liability is correct in proceedings for determination of employment status. *See* § 7436(a); *see also Ewens & Miller, Inc. v. Commissioner*, 117 T.C. 263, 267–68 (2001). Because the denial of a taxpayer's eligibility for VCSP directly affects the amounts of tax, the procedures that Congress has established for judicial review of the Commissioner's determinations logically contemplate review of such a denial as one element of the determination. *See Trimmer,* 148 T.C. at 347; *Estate of Gardner*, 82 T.C. at 996.

We conclude that we have jurisdiction to determine whether the VCSP enters into the computation of petitioner's taxes owed.[1] We will deny respondent's motion.

II. *Petitioner's Motion for Summary Judgment*

Summary judgment may be granted where the pleadings and other materials show that there is no genuine dispute as to any material fact and a decision may be rendered as a matter of law. Rule 121(b); *Sundstrand Corp. v. Commissioner*, 98 T.C. 518, 520 (1992), *aff'd*, 17 F.3d 965 (7th Cir. 1994). The burden is on the moving party to demonstrate that there is no genuine dispute as to any material fact and that the party is entitled to judgment as a matter of law. *FPL Grp., Inc. & Subs. v. Commissioner*, 116 T.C. 73, 74–75 (2001). After reviewing the pleadings and the motion with accompanying exhibits and declarations, we conclude that there is a material dispute regarding the facts.

Petitioner contends that it has met all requirements for participation in the VCSP. Respondent contends that Mr. Treece's misclassification as a nonemployee was uncovered as the result of an employment tax audit. If respondent's argument is correct, petitioner does not meet the participation requirements of the VCSP. We conclude that whether there was an employment tax audit is a dispute of material fact, and therefore we will deny petitioner's Motion for Summary Judgment.

Any contentions we have not addressed are irrelevant, moot, or meritless.

To reflect the foregoing,

An appropriate order will be issued.

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[1] Our review in this case in not contrary to our general policy of not looking behind a statutory notice of determination to examine the Commissioner's motives or conduct in determining a liability because our review is necessary to determine the merits of the Commissioner's determinations. *Estate of Gardner*, 82 T.C. at 1000.

MICHELLE DELPONTE, PETITIONER *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket Nos. 1144-05, 1334-06, 20679-09, 20680-09, 20681-09. Filed May 5, 2022.

P raised innocent-spouse relief as an affirmative defense in a deficiency proceeding. Following IRS procedure, R's counsel referred the request to its Cincinnati Centralized Innocent Spouse Operation (CCISO). CCISO concluded that P was entitled to relief under I.R.C. § 6015(c). CCISO communicated this to R's counsel, who asked P for more information to make a final determination. P instead moved for entry of decision granting her relief. *Held*: Where innocent-spouse relief is raised as an affirmative defense for the first time in a petition that invokes our deficiency jurisdiction, R's counsel has final authority to concede or settle the issue with P. *Held*, *further*, P's motion for entry of decision will be denied.

Alvah Lavar Taylor, *Jonathan T. Amitrano*, and *Lisa O. Nelson*, for petitioner.

Benjamin R. Poor and *Paul Colleran*, for respondent.

OPINION

HOLMES, *Judge*: Michelle DelPonte separated from her ex-husband, William Goddard, in 2000. She is still, more than twenty years later, trying to untangle his affairs from her own. What concerns us is her effort to be relieved of her liability on the joint tax returns she filed with Goddard while they were married. The part of the IRS bureaucracy that usually handles these sorts of requests thinks she's entitled to relief. The IRS's lawyer disagrees. We must decide who speaks for the IRS.

Background

During his marriage to DelPonte,[1] Goddard was a lawyer who sold exceptionally aggressive tax-avoidance strategies with his business partner David Greenberg and became very wealthy in the process. He tried to shelter his income from

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[1] DelPonte's name during the marriage was "Michelle Goddard," and her petitions were filed under that name. She has since remarried and legally changed her name to "Michelle DelPonte," and we have amended the captions in these cases to reflect that change.

selling shelters by using the same shelter strategy he sold, but the IRS soon caught on and issued notices of deficiency for tax years 1999, 2000, and 2001. Most of the facts surrounding Goddard's and Greenberg's schemes—and the audit that led to their notices of deficiency—are irrelevant to these cases. We have already described them in detail in *Greenberg v. Commissioner*, 115 T.C.M. (CCH) 1403 (2018), *aff'd,* 10 F.4th 1136 (11th Cir. 2021), *and aff'd sub nom. Goddard v. Commissioner*, No. 20-73023, 2021 WL 5985581 (9th Cir. Dec. 17, 2021).

What is relevant, though, is the fact that Goddard filed joint returns with DelPonte for each of those three years. That means she is jointly and severally liable with Goddard for the several millions of dollars in tax that we found were owed to the IRS. *See* § 6013(d)(3).[2] So when the first notice of deficiency arrived in late 2004, it was addressed to "William A. and Michelle Goddard." But DelPonte was kept in the dark about this notice. It had been sent to Goddard's law firm, and Goddard—who had by that time been living apart from DelPonte for a few years—never told her. He instead filed a petition on her behalf asserting that she was an "innocent spouse" under section 6015, apparently recognizing that he was solely responsible for the profits he had accumulated over the years and that it was only fair that he should be solely responsible for any large tax bill that might result.

The IRS sent another notice of deficiency to Goddard's law firm in 2005 and three more in 2009. In response to each notice, Goddard filed a petition in which he asserted innocent-spouse relief on DelPonte's behalf without telling her. It wasn't until November 2010 that DelPonte first became aware of the deficiencies asserted against her and the ongoing litigation before us.[3] She promptly hired her own lawyer and ratified the petitions Goddard had filed.

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[2] Unless otherwise indicated, all statutory references are to the Internal Revenue Code, Title 26 U.S.C., in effect at all relevant times, all regulation references are to the Code of Federal Regulations, Title 26 (Treas. Reg.), in effect at all relevant times, and all Rule references are to the Tax Court Rules of Practice and Procedure.

[3] We had in May 2010 already ordered that the litigation should be bifurcated so that we could first decide the amounts of the liabilities owed and then address the issue of whether DelPonte qualified for innocent-spouse relief.

In April 2011 the Office of Chief Counsel referred DelPonte's claim for innocent-spouse relief to the IRS's Cincinnati Centralized Innocent Spouse Operation (CCISO) "to make a determination regarding [DelPonte's] entitlement to such relief." CCISO is the IRS unit that receives and processes most requests for innocent-spouse relief. Internal Revenue Manual (IRM) 25.15.3.3 (Dec. 12, 2016).[4] Its determination letters are generally binding on the Commissioner and the spouse asking for relief, *see* IRM 25.15.18.1.1(2) (Mar. 20, 2019), but the referral letter that accompanied DelPonte's request asked CCISO to not issue a determination letter but instead "provide the results of [its] consideration directly to [the Office of Chief Counsel]." Having received the referral, CCISO reached out to DelPonte directly and instructed her to fill out and return a Form 8857, Request for Innocent Spouse Relief. DelPonte did just that, and after reviewing her paperwork, CCISO concluded in December 2011 that she should be granted relief for each of the years at issue.

CCISO did what the Chief Counsel lawyer had asked. It did not send a determination letter to DelPonte, but instead sent a letter explaining its conclusion directly to the Office of Chief Counsel. And here's where an already unusual case got even more unusualer. Rather than accepting CCISO's conclusion and settling DelPonte's cases, the Office of Chief Counsel "decided that more information was needed . . . to allow [DelPonte] relief under I.R.C. [section] 6015." So in August 2012 the Office of Chief Counsel invited DelPonte to participate in a *Branerton*[5] conference to exchange documents and information "[i]n order for [CCISO] to properly evaluate [her] claim for relief." It also informed her that CCISO had already "rendered its decision in [her favor], but that [the Office of Chief Counsel] had overridden that decision." DelPonte declined the invitation; she argued that additional information would be superfluous because CCISO had already decided she was

[4] The IRM doesn't have the force of law or confer substantive rights on taxpayers. It does, however, govern the internal affairs and administration of the IRS, and reliably describes the functions delegated to the different offices within the IRS. *United States v. McKee*, 192 F.3d 535, 540 (6th Cir. 1999).

[5] *Branerton Corp. v. Commissioner*, 61 T.C. 691 (1974) (describing Tax Court's informal discovery procedure).

entitled to relief and that its decision was binding on Chief Counsel.

Aside from some back-and-forth letters between DelPonte and Chief Counsel in which they argued the point, that's where things stood for many years. In the meantime the consolidated deficiency cases begun by Goddard and Greenberg progressed through discovery, trial, and briefing. We released our opinion in those cases in May 2018, and in it we upheld the Commissioner's determinations of deficiencies in all respects except where he failed to meet the supervisory-approval requirement of section 6751(b). *Greenberg*, 115 T.C.M. (CCH) at 1418. We ordered the parties to compute the correct amounts of tax owed under Rule 155, but in cases as complex as these, that task isn't as simple as plugging numbers into a calculator and getting a total—the parties spent more than a year to precisely calculate the deficiencies. We severed the five cases in which DelPonte was a petitioner in January 2020, and entered decisions in the remaining ten the following April. Goddard and Greenberg then appealed their cases to the Eleventh Circuit in August 2020. Goddard's cases were severed from Greenberg's and transferred to the Ninth Circuit the following October.[6] The Eleventh Circuit affirmed our holdings in Greenberg's cases, *Greenberg*, 10 F.4th 1136, in August 2021 and the Ninth Circuit did likewise in December, *Goddard*, 2021 WL 5985581. So nearly fifteen years after the lowest numbered cases in that group had first been calendared for trial, they are now final and unappealable.

DelPonte and Chief Counsel resumed their correspondence on the innocent-spouse issue shortly after we released our opinion in the deficiency cases. DelPonte hired a new team of lawyers and responded to the Chief Counsel's discovery requests, but still insisted that discovery was unnecessary because CCISO had already granted her relief. Chief Counsel stood firm in its position that CCISO didn't speak for the IRS in her cases. DelPonte then moved for entry of decisions in her favor because, in her view, Chief Counsel is wrong.

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[6] Greenberg lived in Florida when he filed his petitions, so the venue for appeal of his cases was the Eleventh Circuit. *See* § 7482(b)(1). Goddard lived in California at the time, so the venue for appeal in his cases was the Ninth Circuit. *See id.* Because DelPonte also lived in California when the petitions in her cases were filed, venue for appeal of her cases would also be in the Ninth Circuit. *See id.*

We usually get motions for entry of decision when a party wants to renege on a settlement or when parties disagree about computations under Rule 155. In these cases, however, there is no stipulation or computation to fight about. This motion is really more like one for partial summary judgment on the issue of whether DelPonte is entitled to relief under section 6015(c) because the CCISO determined that she is.

And that is how we will treat it.

Discussion

This is a novel argument, and to analyze it we will begin with an account of the evolution of the different species of innocent-spouse relief. Congress has since 1918 allowed married taxpayers to file joint returns, Revenue Act of 1918, ch. 18, § 223, 40 Stat. 1057, 1074 (1919); *see also Camara v. Commissioner*, 149 T.C. 317, 327 (2017), and has since 1938 held spouses jointly and severally liable for the tax shown on those joint returns, Revenue Act of 1938, ch. 289, § 51(b), 52 Stat. 447, 476; *see also Wilson v. Commissioner*, 705 F.3d 980, 982 (9th Cir. 2013), *aff'g* 99 T.C.M. (CCH) 1552 (2010). A great many couples benefited richly from the more favorable tax rates available to joint filers, but some were burdened by the harsh consequences of joint liability. *See Wilson*, 705 F.3d at 983. We commented on the harshness of this rule in *Scudder v. Commissioner*, 48 T.C. 36 (1967), *remanded by* 405 F.2d 222 (6th Cir. 1968), when we held a wife liable for tax on the money her husband had embezzled from the partnership she and her sisters owned and that he had unsurprisingly failed to report on their joint returns.[7] We found that the language of the statute was clear, and that "only remedial legislation can soften the impact of the rule of strict individual liability." *Id.* at 41.[8]

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[7] On appeal, the Sixth Circuit noted that "'trickery' or 'deliberate deception,' employed by [a] husband to obtain his wife's signature to a tax return, will exonerate the victimized wife." *Scudder*, 405 F.2d at 226. It then ordered us to reexamine our findings while considering whether at least some of the embezzled funds should have more properly been treated as a nontaxable loan to the husband because that was how they were recorded in the partnership's books and because he paid back about half of what he took soon after his wrongdoing was discovered. *See id.* at 225.

[8] Two exceptions to this strict rule were that a spouse wouldn't be held jointly and severally liable if there had been duress, *see, e.g.*, *Furnish*

In 1971 Congress enacted legislation to allow a spouse relief from joint and several liability in certain limited situations. Act of January 12, 1971, Pub. L. No. 91-679, 84 Stat. 2063 (codified at § 6013(e)). Relief got a little easier in 1984, *see* Deficit Reduction Act of 1984, Pub. L. No. 98-369, § 424, 98 Stat. 494, 801 (codified at § 6013), but it still required that a spouse seeking relief show that the joint return showed "a substantial understatement of tax attributable to grossly erroneous items of [the other] spouse," that she signed the return without knowing and without having reason to know of the substantial understatement, and that it would be inequitable to hold her liable for the deficiency attributable to the substantial understatement, *id.* Neither Congress nor the Secretary wed this substantive liberalization to any special procedural rules for requesting relief. *See Corson v. Commissioner*, 114 T.C. 354, 358 (2000); T.D. 7320, 1974-2 C.B. 391. The result was that spouses glommed their requests for relief onto petitions to redetermine deficiencies that they filed in our Court or onto complaints for refund filed in a U.S. district court. *See Corson*, 114 T.C. at 358.

Congress liberalized the innocent-spouse-relief provisions again as part of the IRS Restructuring and Reform Act of 1998 (RRA 1998), Pub. L. No. 105-206, § 3201, 112 Stat. 685, 734 (codified as amended at § 6015). Under new section 6015, relief was available even if the understatement was not "substantial" or due to "grossly erroneous" items. Requesting spouses[9] could seek any of three types of relief. The first requires:

- an understatement of tax on the joint return that is attributable to erroneous items of the other spouse;
- that the requesting spouse didn't know or have reason to know of the understatement when she signed the return;
- that, "taking into account all the facts and circumstances, it [would be] inequitable to hold [that spouse] liable for

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v. Commissioner, 262 F.2d 727 (9th Cir. 1958), or fraud, *see, e.g.*, *Sharwell v. Commissioner*, 419 F.2d 1057 (6th Cir. 1969).

[9] Section 6015 speaks of a spouse who "elects" the application of subsections (b) and (c), and "requests" relief under subsection (f). A spouse seeking relief under any of the three subsections is nevertheless commonly referred to as a "requesting spouse." *E.g.*, Treas. Reg. § 1.6015-5(a).

the deficiency . . . attributable to such understatement;" and
- that the requesting spouse seek relief no later than two years after the Commissioner began collection activities.

§ 6015(b).

The second requires the requesting spouse to:

- be legally separated or divorced from the nonrequesting spouse at the time of election; and
- have no actual knowledge of any items giving rise to a deficiency at the time she signed the return.

§ 6015(c).

And then there is the catchall third type that requires proof only that, "taking into account all the facts and circumstances, it [would be] inequitable to hold the [requesting spouse] liable for any unpaid tax or any deficiency," and that the requesting spouse is not eligible for either of the other two types of relief. § 6015(f).

These are known by those who have lettered in innocent-spouse relief as "b", "c", and "f" relief. And each of these three letters can be paired with three paths to Tax Court:

- as an issue—usually called a "defense" even though raised by a petitioner—in a deficiency case;
- in an action to review the IRS's determination in a collection-due-process (CDP) case, a new right also created by RRA 1998; or
- in a "stand alone" action in which we review the IRS's administrative determination made in response to a request for relief filed by a spouse directly with the IRS.

We've already outlined a bit of the history of innocent-spouse relief in deficiency cases. To place DelPonte's argument in the proper context, we need to sketch a bit of background for our expanded jurisdiction in CDP and stand-alone innocent-spouse cases.

RRA 1998 created CDP procedures to enable taxpayers to challenge how the Commissioner collected taxes that he assessed. *See* RRA 1998 § 3401, 112 Stat. at 746 (codified as amended at §§ 6320, 6330). This new CDP right made for a major change in the way the IRS used two of its most important collection tools—liens and levies. Once a taxpayer's liability has been assessed, the amount of the liability becomes a lien in favor of the government. § 6321. When that happens, the Commissioner sends the taxpayer a notice of federal tax lien (NFTL), informing him that the lien has been filed and, under RRA 1998, of his right to request a CDP hearing. § 6320. If the Commissioner wishes to collect tax by seizing a taxpayer's property he must now also send him a notice of intent to levy, which, like the NFTL, informs him of his right to a CDP hearing. § 6330. Congress wedded innocent-spouse relief to CDP law by specifically providing that a spouse could raise entitlement to innocent-spouse relief in a CDP hearing. Regulations provide that when a taxpayer raises innocent-spouse relief in a CDP hearing, the innocent-spouse issue is "governed in all respects by the provisions of . . . section 6015 and the regulations and procedures thereunder." Treas. Reg. §§ 301.6320-1(e)(2), 301.6330-1(e)(2).

Then there's our jurisdiction in stand-alone cases. A spouse may also ask for innocent-spouse relief outside a deficiency case or a CDP hearing. If she does, and if the Commissioner denies her relief, she may, "[i]n addition to any other remedy provided by law, . . . petition [us] (and [we] shall have jurisdiction) to determine the appropriate relief available" under section 6015. § 6015(e)(1)(A).

Congress wanted a requesting spouse to have only one bite from any of these three legal apples. A requesting spouse is "entitled to only one final administrative determination of relief" for a given assessment. Treas. Reg. § 1.6015-5(c)(1). And once we (or a district court) have rendered a final decision on her eligibility for relief—or if she "participated meaningfully" in a court proceeding and chose not to raise a request for relief—then that spouse is barred from relief thereafter. *See* § 6015(g)(2).

We can now classify DelPonte's request with precision. It is for "c" relief in a deficiency case. But whether it is "b", "c", or "f" relief in a deficiency, CDP, or stand-alone case, a requesting spouse has to navigate her way through the ever more detailed revenue procedures and regulations that the Secretary started to issue after section 6015's enactment. This journey begins with the Form 8857. T.D. 9003, 2002-2 C.B. 294. The regulation requires a requesting spouse to file a Form 8857; submit a written statement containing the same information required by Form 8857; or "submit information in the manner prescribed by the Treasury and IRS in forms, relevant revenue rulings, revenue procedures, or other published guidance." Treas. Reg. § 1.6015-5(a). A requesting spouse can do this any time after the Commissioner sends her notice of an audit or a letter that tells her there may be an outstanding liability, *id.* para. (b)(5), but no later than two years after the Commissioner initiates collection activity, *id.* subpara. (1).[10] A single claim can simultaneously request relief under section 6015(b), (c), and (f). *Id.* para. (a)(2).

But if the Code is now clear that a spouse has these ways to ask for three kinds of innocent-spouse relief, it is still murky about who gets to act on those requests and whether that answer differs according to which of the three ways a spouse chooses.

We begin with the Code. Section 7803 creates the position of Commissioner of Internal Revenue, to whom are given broad powers to "administer, manage, conduct, direct, and supervise the execution and application of the internal revenue laws or related statutes," as well as any other "such duties and powers as the Secretary may prescribe." § 7803(a)(2). Regulations authorize the Secretary of the Treasury to delegate any function vested in him to the Commissioner, who is in turn authorized to redelegate that function to an officer or employee under his direct or indirect supervision and control. Treas. Reg. § 301.7701-9(b) and (c). The Secretary has of course for decades delegated to the Commissioner the responsibility of administering and enforcing the internal revenue laws, I.R.S. Treas. Order 150-10 (Apr. 22, 1982),

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[10] We have held the two-year limitations period is invalid as to requests for equitable relief under section 6015(f). *Pullins v. Commissioner*, 136 T.C. 432 (2011). The Secretary hasn't revised his regulations, *see* Treas. Reg. § 1.6015-5(a), and the limitations period remains valid for elections under section 6015(b) and (c), *see Pullins*, 136 T.C. at 437. The Seventh Circuit, however, has disagreed with us about the validity of this two-year limitations period. *See Lantz v. Commissioner*, 607 F.3d 479, 482 (7th Cir. 2010) ("that Congress designated a deadline in two provisions of the same statute and not in a third is not a compelling argument that Congress meant to preclude the Treasury Department from imposing a deadline applicable to cases governed by that third provision").

which includes making determinations about whether a taxpayer is entitled to innocent-spouse relief under section 6015, *see* § 6015(e)(1)(A)(i), (5), (f). The Commissioner has redelegated the responsibility for processing most requests for innocent-spouse relief to the CCISO. IRM 25.15.7.1 (Sept. 1, 2006). There are some exceptions: In certain instances, as when there's an ongoing audit for the year for which the requesting spouse is seeking relief, the Field Examination unit conducting the audit has authority to make the determination. *See* IRM 25.15.6.1(4) (Mar. 21, 2008). Once CCISO (or the Field Examination unit) has made a preliminary determination, both the requesting spouse and the nonrequesting spouse can appeal the determination to the Office of Appeals.[11] IRS Appeals is responsible for holding an appeals conference, reviewing the evidence, and issuing a "final determination." IRM 25.15.6.10.3 (June 19, 2017). Or maybe we should say a final *administrative* determination because if Appeals denies her request, a requesting spouse[12] can petition our Court for a really *truly* final determination of her entitlement to relief. § 6015(e). We ourselves can make a determination of our own if CCISO or the Field Examiner doesn't act on a request within six months. § 6015(e)(1)(A).

There is a similarly complicated process when a spouse seeks relief as part of a CDP hearing. She has to first file a Form 12153, Request for a Collection Due Process or Equivalent Hearing (or other written and signed request), with IRS Appeals. IRM 5.19.8.4.2 (Nov. 1, 2007). That form allows her to check a box to claim innocent-spouse relief and, if she does, instructs her to attach a Form 8857. *See* Form 12153 (Rev. Nov. 2006). IRS Appeals ordinarily sends the Form 8857 to CCISO to investigate the claim, *see* IRM 8.22.1.1.1.5.3 (Oct. 19, 2007), following the same procedures as it would in a standalone innocent spouse case, *see* IRM 8.22.2.2.11.3(6) (Jan. 1, 2006). A significant difference, though, is that Appeals retains jurisdiction over the case while CCISO investigates the claim. *See id.* 8.22.2.2.11.3(4). One consequence of this is that CCISO ordinarily doesn't make a *final* determination on what

[11] Recently renamed the "Independent Office of Appeals." *See* Taxpayer First Act, Pub. L. No. 116-25, § 1001(a), 133 Stat. 981, 983 (2019).

[12] But not a nonrequesting spouse. *Maier v. Commissioner*, 119 T.C. 267 (2002), *aff'd*, 360 F.3d 361 (2d Cir. 2004).

relief is appropriate. *See* IRM 8.22.2.2.11.3.1 and .2 (Mar. 11, 2009). CCISO instead *recommends* a determination to Appeals, which is itself responsible for making a final determination about what relief if any a taxpayer should get. *Id.*[13] A disgruntled requesting spouse can once again petition us to try again. § 6015(e)(1)(A).

These paths are well trod. And they may help us in the unusual situation in DelPonte's case: where we have a requesting spouse who raised innocent-spouse relief as an affirmative defense in deficiency petitions filed under section 6213(a). DelPonte argues that the Secretary has delegated authority to make a final determination to the administrative, not the litigating, side of the IRS. She has a textualist argument based on the regulations, numerous IRM provisions, the Chief Counsel's own written guidance, and even the instructions to the Form 8857. She also argues more purposively that her position is buttressed by the principles of horizontal equity and fundamental fairness. In short, she contends that it's only fair that a requesting spouse raising innocent-spouse relief for the first time in litigation should have CCISO make the determination, just as if she had raised it for the first time in a stand-alone request. According to her CCISO is the decider in chief, and Chief Counsel's job is only to defend CCISO's determination.

The Chief Counsel, on the other hand, argues that his office is responsible for deciding what positions the IRS takes in litigation, and that decision about whether to concede innocent-spouse relief is a litigating position. He of course may ask CCISO for its advice, but he says he gets the final say.

The Chief Counsel is right that he and his lawyers are responsible for the IRS's litigation decisions. Section 7803—the same section that's the source of the Commissioner's authority—also created the position of Chief Counsel, and authorized him to "perform such duties as may be prescribed by the Secretary, including the duty . . . to represent the Commissioner in cases before the Tax Court." § 7803(b)(2)(D). General

[13] As always seems to be the case in tax law, there is a complication: The CCISO can itself make a final determination if it concludes the requesting spouse should get relief *and* the nonrequesting spouse doesn't appeal the determination *and* innocent-spouse relief was the only issue raised in the CDP request *and* the requesting spouse chooses to withdraw the CDP request *and* she waives any right to judicial review. *See* IRM 8.22.2.2.11.3.1.

Counsel Order No. 4 delegates to the Chief Counsel authority "in cases pending in the Tax Court . . . to decide whether and in what manner to defend, or to prosecute a claim, or to settle, or to abandon a claim or defense therein." *See* IRM 30.2.2–.6 (Aug. 11, 2004). This order also gives the Chief Counsel the authority to redelegate any of his authority to "any officer or employee in the Office of the Chief Counsel, and to authorize further redelegation of such authority." *Id.*

The question we must answer, then, is whether DelPonte's request for innocent-spouse relief—and CCISO's consideration of that request—was like any claim in a case "pending in Tax Court," or more like an administrative request for innocent-spouse relief begun by filing a Form 8857 with CCISO.

This is a question in which a page of history enlightens us more than a volume of logic. Taxpayers were raising innocent-spouse claims as affirmative defenses in deficiency proceedings years before today's administrative processes for seeking relief even existed. Our jurisdiction to rule on those claims is part of our authority under section 6213(a) to redetermine a taxpayer's deficiency when she's received a notice of deficiency. *See Corson*, 114 T.C. at 363–64 ("In a deficiency proceeding, we may take into account all facts and circumstances relevant to ascertaining the correct amount of the deficiency, including affirmative defenses"). Our power in a deficiency case is not limited to the issues listed in the notice of deficiency—it includes issues raised in either the petition or answer or even those tried without objection. *See Ax v. Commissioner*, 146 T.C. 153, 160 (2016). Our jurisdiction to decide an issue in a deficiency case is not dependent on the Commissioner's having already made a determination on that issue administratively; all we need to get jurisdiction to decide is a timely filed petition and a valid notice of deficiency. *Butler v. Commissioner*, 114 T.C. 276, 288 (2000) (citing *Naftel v. Commissioner*, 85 T.C. 527, 533 (1985)). Once we have jurisdiction over a case where entitlement to innocent-spouse relief is an issue, the Commissioner must concede or settle it with a taxpayer if he doesn't want to litigate it. Section 7803(b)(2) and related delegation orders have long delegated those decisions to the Chief Counsel.

But the Chief Counsel also has the power to redelegate authority granted to him. *See* IRM 30.2.2–.6. DelPonte argues in the alternative that Chief Counsel Notice CC-2009-021 (June 30, 2009) is just such a redelegation. That notice instructs attorneys in the Office of Chief Counsel to request CCISO "to make the determination" with respect to cases in which a taxpayer raises innocent-spouse relief for the first time in a deficiency petition. CC-2009-021, at 2. That notice also states: "If CCISO . . . determines the petitioner is entitled to relief, the case should be conceded . . . subject to the limitation that a nonrequesting spouse who is a party to the case must agree" with the determination. *Id.* at 4. If the nonrequesting spouse disagrees, then "the grant of relief must be defended throughout trial and briefing." *Id.*

We can dispense with this argument quickly. Chief Counsel has authority to delegate functions only to an "officer or employee in the Office of the Chief Counsel," IRM 30.2.2–.6, and CCISO is not within the Office of the Chief Counsel, IRM 1.1.13.12.3.3 (Sept. 1, 2005). The plain language of this order gives the Chief Counsel no authority to delegate any of his functions to CCISO.

But we can reformulate DelPonte's contention just a bit: Even though Chief Counsel has responsibility to respond to requests for relief raised for the first time in a deficiency case, he has instructed his lawyers to adhere to CCISO determinations. Are his lawyers going rogue if they disregard this instruction? This is not an argument based on powers of delegation, but on what DelPonte identifies as a possible protection of the Due Process Clause—a requirement that the government follow the procedures that it establishes even if it didn't have to establish them in the first place. DelPonte emphasizes that she doesn't raise this issue in her present motion, but we can head off future motion practice by noting that the Chief Counsel attorneys handling these cases *have* been following established procedures.

We first address DelPonte's argument that CC-2009-021 instructs Chief Counsel attorneys to refer cases to CCISO for a "determination," not a "recommendation." She relies heavily on the text of CC-2009-021—along with the Chief Counsel attorney's correspondence with her and CCISO—to argue that "determinations" cannot be disregarded by Chief Counsel attorneys. We, however, are not convinced that use of the word "determination" in the Chief Counsel notice or any other guidance is the same as what the regulation calls a "final administrative determination." *See* Treas. Reg. § 1.6015-5. We have long recognized that "the name or the label of a document does not control whether the document embodies a determination." *Wilson v. Commissioner*, 131 T.C. 47, 53 (2008).

In CC-2009-021, the Chief Counsel repeatedly uses "should" when instructing his attorneys on how to handle cases where CCISO determines that relief should be granted, e.g., "[i]f CCISO . . . determines the petitioner is entitled to relief, the case *should* be conceded." CC-2009-021, at 4 (emphasis added). But he elsewhere uses the imperative "must" when describing how an attorney should proceed in different circumstances, e.g., "[i]f the nonrequesting spouse disagrees with the Service's determination to grant relief [to the requesting spouse], then . . . the grant of relief *must* be defended throughout trial and briefing." *Id.* (emphasis added). If Chief Counsel had wanted all his attorneys to accept CCISO's determinations in every case, he could easily have conveyed that desire by telling them they "must" do so. But he did not.

CC-2009-021 is, moreover, only one of a series of notices that deal with requests for innocent-spouse relief raised for the first time in cases pending before us. CC-2009-021 was itself a supplement to the earlier Chief Counsel Notice CC-2004-26 (July 12, 2009), *id.* at 1, which was issued in response to our holding in *Ewing v. Commissioner*, 122 T.C. 32 (2004), *rev'd and vacated*, 439 F.3d 1009 (9th Cir. 2006). We held in *Ewing* that, although we reviewed the Commissioner's denial of equitable relief under section 6015(f) for abuse of discretion, our review was not confined to the administrative record. *Ewing*, 122 T.C. at 38–39. CC-2004-26 included instructions for how Chief Counsel attorneys should handle section 6015(f) cases to keep the scope-of-review issue alive for appeal. CC-2004-026, at 1–2. It also sought to solve the problem of how to handle requests for equitable relief that were raised for the first time before us—either in deficiency petitions or after six months had passed since the taxpayer requested relief—and in such cases there *would be no* administrative record to review. His solution was to have those cases remanded to CCISO for a determination and to create an administrative record. *Id.* at 3. The notice told CCISO to "send all evidence the petitioner presented . . . and its written analysis to the Chief Counsel attorney handling the docketed case. If CCISO determines the petitioner is entitled to relief, the Chief Counsel attorney *should consider* whether settlement is appropriate." *Id.* at 4 (emphasis added).

CC-2009-021 itself was prompted by our opinions in *Porter v. Commissioner* (*Porter I*), 130 T.C. 115 (2008), and *Porter v. Commissioner* (*Porter II*), 132 T.C. 203 (2009), CC-2009-021, at 1, in which we held that we would conduct trials *de novo* in innocent-spouse cases, *Porter I*, 130 T.C. at 125, and make our own determinations about relief under section 6015(f) with no deference to the IRS, *Porter II*, 132 T.C. at 210. Like its predecessor, CC-2009-021 provided guidance to the Chief Counsel lawyers on how to preserve these issues for appeal. CC-2009-021, at 2. It also told Chief Counsel attorneys that they should continue asking CCISO to make determinations in all section 6015 cases, and they should continue to concede cases where CCISO determined the requesting spouse was entitled to relief. *Id.* at 2–4.

Chief Counsel Notice CC-2013-011 (June 7, 2013), issued after *Wilson*, 705 F.3d 980, confirmed that section 6015(e)(1)(A) provided for both a *de novo* standard *and* scope of review in section 6015(f) cases, and rendered both these older notices obsolete.[14] This notice was published after CCISO had already rendered its decision on DelPonte's request, but we believe it is still helpful in understanding the Chief Counsel's guidance that was in effect. CC-2013-011 again requires that Chief Counsel attorneys request a determination from CCISO where a petitioner requests relief under any provision of section 6015. CC-2013-011, at 1–2. It also clarifies that "the trial attorney *should, except in rare circumstances*, follow the determination made by CCISO that the petitioner is entitled to relief and settle the case in accordance with CCISO's determination." *Id.* at 3 (emphasis added). The "should" instead of a "must" means that in this context the CCISO's decisions are advisory, and that Chief Counsel attorneys get to make the final decision about the IRS's views on any particular request

[14] Congress eventually settled the issue when it decided that we should review the IRS *de novo* based upon the administrative record and "any additional newly discovered or previously unavailable evidence." Taxpayer First Act § 1203(a)(1), 133 Stat. at 988 (codified at § 6015(e)(7)).

for innocent-spouse relief when a taxpayer seeks it in a deficiency case.

And let us zoom out to look one last time at the IRM. It says that if innocent-spouse relief is raised for the first time in a case already docketed in court, "[j]urisdiction is retained by . . . Counsel, and a request is sent to CCISO to consider the request for relief." IRM 25.15.12.25.2(1) (Nov. 9, 2007). It specifies that "Counsel . . . has functional jurisdiction over the matter and handles the case and request for relief, and either settles or litigates the issue on its merits, as appropriate." *Id.* 25.15.12.25.2(3).

We therefore hold that the Chief Counsel notices and the IRM all tell CCISO to provide "assistance," not to make a final determination, and that Chief Counsel attorneys retain their discretion to adopt or reject CCISO's conclusions.

We finally address DelPonte's argument that principles of horizontal equity and "fundamental fairness" require that all taxpayers be entitled to a final determination of relief from CCISO, regardless of whether they first request relief in a petition for redetermination of a deficiency, in a stand-alone petition, or in a CDP hearing. She correctly points out that taxpayers often have no choice in when they are first able to request relief—her case is an excellent example. She believes that adopting the position of the Office of Chief Counsel would put requesting spouses who first raise innocent-spouse relief in a petition for redetermination of a deficiency in a materially worse position than all other requesting spouses because all other requesting spouses have the opportunity to appeal a denial of relief by CCISO to Appeals before starting a case with us as a last resort. Is it not unfair that some who seek relief can have a try at CCISO, Appeals, and Tax Court, but others get Tax Court alone?

Arguments from fairness are always fragile, and this one breaks apart for two reasons. The first is its faulty premise—an Appeals officer who receives a request for innocent-spouse relief in a CDP hearing forwards the case to CCISO for processing but retains jurisdiction, *see* IRM 8.22.2.2.11.3(4), and makes the ultimate decision for the IRS about whether to grant relief, *see* IRM 8.22.2.2.11.3.1–.2. In that sense, the Appeals officer's role is very similar to that of the Chief Counsel attorney in deficiency cases—the difference, of course, being that the Appeals officer can make a final determination granting relief, whereas a Chief Counsel attorney can only decide not to argue that we should deny relief. So a requesting spouse who raises an innocent-spouse claim for the first time in a CDP hearing really gets only two levels of review—Appeals and us—not three. Requiring CCISO to have the opportunity to issue a final determination in cases where the requesting spouse raises an innocent-spouse claim for the first time in a deficiency petition would therefore not guarantee that all spouses be treated equally regardless of when they request relief; it would merely make CDP cases the outlier.

The second and more important problem with this argument is that we have no power to adopt it. Congress gave us exclusive jurisdiction to redetermine the correct amount of a taxpayer's deficiency for a given tax year once the taxpayer receives a valid notice of deficiency and timely files a petition with us. *See* § 6213(a); *Naftel*, 85 T.C. at 532–33. Congress also gave the Chief Counsel the authority to litigate cases before us. § 7803(b)(2)(D). We cannot undo this statutory scheme by depriving either ourselves or the Chief Counsel of the powers it has given to us in the name of fairness.

The Chief Counsel in these cases has considered the determination of CCISO to grant DelPonte relief and decided not to adopt it without further investigation. That is his prerogative, and we will not force him to do otherwise.

An appropriate order will be issued.

ANGELA M. CHAVIS, PETITIONER *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 11835-20L. Filed June 15, 2022.

During 2011–2014 P and her then husband were officers of a corporation that withheld payroll taxes from its employees' wages but did not pay those taxes over to the Government. R issued a Letter 1153, Notice of Trust Fund Recovery Penalty, informing P that he intended to assert trust fund recovery penalties (TFRPs) against her and her husband under I.R.C. § 6672. P did not challenge the proposed assessment, as she was entitled to do, and R thereafter assessed TFRPs totaling $146,682. In an effort to collect this unpaid liability

R issued P a Letter 3172, Notice of Federal Tax Lien Filing and Your Right to a Hearing. P timely requested a collection due process (CDP) hearing. During the CDP hearing P sought to challenge her underlying liability for the TFRPs. R explained that P could not challenge her underlying liability because she had, but declined to take advantage of, a prior opportunity to challenge the TFRPs upon receipt of the Letter 1153. P requested "innocent spouse" relief under I.R.C. § 6015, but R determined that such relief is unavailable for TFRP liabilities. Finally, P requested that her account be placed in "currently not collectible" status and that the lien be withdrawn. R considered these collection alternatives but determined that P did not qualify for either one. R issued a notice of determination sustaining the lien filing, and P timely petitioned this Court. *Held*: Because P had a prior opportunity to challenge her TFRP liability upon receipt of the Letter 1153, she was not entitled to challenge her underlying tax liability at the CDP hearing or in this Court. *Held*, *further*, R correctly determined that P was not eligible for "innocent spouse" relief under I.R.C. § 6015 because her TFRP liability did not arise from any liability shown on a joint Federal income tax return. *Held*, *further*, R did not abuse his discretion in sustaining the collection action.

Angela M. Chavis, pro se.
Catherine S. Tyson, for respondent.

OPINION

LAUBER, *Judge*: In this collection due process (CDP) case petitioner seeks review pursuant to sections 6320(c) and 6330(d)(1) of the determination by the Internal Revenue Service (IRS or respondent) to uphold the filing of a Notice of Federal Tax Lien (NFTL).[1] Petitioner challenges her underlying tax liability, seeks "innocent spouse" relief, and contends that the IRS improperly denied her request to have her account placed in "currently not collectible" (CNC) status. Respondent has moved for summary judgment, contending that petitioner's underlying liability is not properly before us, that section 6015 does not apply to the tax liability at issue, and that the settlement officer did not abuse her discretion in sus-

[1] Unless otherwise indicated, all statutory references are to the Internal Revenue Code, Title 26 U.S.C., in effect at all relevant times, and all regulation references are to the Code of Federal Regulations, Title 26 (Treas. Reg.), in effect at all relevant times. We round all monetary amounts to the nearest dollar.

taining the collection action. We agree and accordingly will grant the motion.

Background

The following facts are derived from the parties' pleadings and motion papers, including a declaration that attached the administrative record. Petitioner resided in Missouri when she timely petitioned this Court.

Petitioner received a B.A. in economics and an M.A. in business administration, having completed coursework in finance, accounting, marketing, management, and organizational behavior. At the relevant times she and her then husband were associated with Oasys Information Systems, Inc. (Oasys), a C corporation established in 2008. Her then husband was the president of Oasys, and she held the office of secretary. According to IRS records, Oasys listed petitioner's home address as its business address.

Oasys withheld payroll taxes from its employees' wages but did not pay those taxes over to the Government. Having no success in collecting these taxes from Oasys, the IRS determined penalties against petitioner and her then husband under section 6672. That section provides that "[a]ny person required to collect, truthfully account for, and pay over" payroll taxes, who willfully fails to do so, shall be liable for a penalty "equal to the total amount of the tax evaded . . . or not accounted for and paid over." § 6672(a). Penalties determined under section 6672 are commonly called trust fund recovery penalties (TFRPs).

On July 13, 2015, the IRS issued petitioner Letter 1153, Notice of Trust Fund Recovery Penalty. The IRS sent this letter by certified mail to petitioner at her home address. Respondent has supplied a copy of U.S. Postal Service (USPS) Form 3811, Domestic Return Receipt, showing that petitioner received and accepted delivery of the Letter 1153 on July 16, 2015. Petitioner does not dispute that the signature on the Form 3811 is her signature.

Attached to the Letter 1153 was Form 2751, Proposed Assessment of Trust Fund Recovery Penalty. This form advised petitioner that Oasys had failed to pay over employment taxes totaling $146,682 for nine calendar quarters during 2011–2014. The IRS proposed to assess that sum against petitioner, determining that she, "[a]s Secretary, . . . had the responsibility of paying the employment taxes [but] paid other creditors over the US Gov't." The IRS proposed to assess joint and several liability for the same amount against her then husband, determining that he, "[a]s President, . . . had the responsibility of paying the employment taxes [but] paid other creditors over the US Gov't."

The Letter 1153 informed petitioner: "You may appeal your case to the local Appeals Office." The letter included detailed instructions about the steps petitioner needed to take in order to appeal the proposed assessment and the issues that would be considered during the appeal. The letter warned: "If we do not hear from you within 60 days from the date of this letter . . . , we will assess the penalty and begin collection action."

Petitioner did not appeal the notice of proposed assessment. On November 16, 2015, the IRS accordingly assessed the TFRPs against her. Petitioner and her husband divorced in 2016, and the IRS was apparently successful in collecting a portion of the unpaid tax from him. In an effort to collect the balance of the liability, the IRS on May 16, 2019, issued petitioner a Letter 3172, Notice of Federal Tax Lien Filing and Your Right to a Hearing. This letter showed an aggregate unpaid balance of $126,919 on account of Oasys's payroll tax liability.

On May 29, 2019, petitioner timely requested a CDP hearing. In her hearing request she checked the boxes, "I cannot pay balance" and "Innocent Spouse Relief," and she requested withdrawal of the NFTL. She urged that her ex-husband was responsible for Oasys's payroll taxes, asserted that she "never received a notice for these taxes before," and contended that she "d[id] not make enough income to put a dent in the amount presented."

In July 2019 petitioner submitted Form 8857, Request for Innocent Spouse Relief. She sought relief from the TFRPs, alleging that she "had no dealings with Oasys." She stated that she "agreed to sign our 1040 tax return jointly [but] never signed any returns from Oasys." She did not request relief from any joint Federal income tax liability.

The IRS Cincinnati Centralized Innocent Spouse Operation (CCISO) processed petitioner's Form 8857 on July 26, 2019. On August 14, 2019, CCISO informed petitioner that she did not "meet the basic eligibility requirements" for relief under section 6015. CCISO explained that she did not qualify for relief because "[s]ection 6015 applies to jointly filed income tax returns," not payroll tax liabilities.

Petitioner's CDP case was then assigned to a settlement officer (SO) in the IRS Independent Office of Appeals (Appeals) in Houston, Texas. The SO reviewed CCISO's file, verified that the TFRPs had been properly assessed, and confirmed that all other legal and administrative requirements had been met. The SO scheduled a telephone conference for November 19, 2019. Petitioner participated in the telephone conference as scheduled.

During the conference the SO explained that section 6015 relief was not available for TFRP liabilities. The SO also advised that petitioner could not now challenge her liability for the TFRPs because she had, but declined to take advantage of, a prior opportunity to challenge them upon receipt of the Letter 1153. Although petitioner said she did not recall receiving that letter, the SO drew her attention to her signature on the USPS Form 3811, which confirmed her receipt of the proposed assessment.

The SO and petitioner then discussed collection alternatives. The SO advised that, if petitioner wished to pursue CNC status, she needed to supply a completed Form 433–A, Collection Information Statement for Wage Earners and Self-Employed Individuals, together with supporting financial information. Petitioner submitted this information, and the SO referred it to an IRS collection specialist for analysis.

On January 30, 2020, the SO received a response from the collection specialist, who concluded that petitioner could pay $2,831 per month toward her TFRP liability and thus did not qualify for CNC status. The SO called petitioner that same day and went over the results of the specialist's computations. Petitioner disputed those calculations, urging that her income had been reduced and that home mortgage payments of $1,611 should be included in her monthly expenses. Petitioner supplied copies of her current pay stubs and mortgage statement to support her position.

On April 7, 2020, the SO recomputed petitioner's ability to pay. The SO calculated her revised monthly income as $5,361, including child support payments of $1,400. Employing an "allowable expense calculator," the SO adjusted petitioner's claimed monthly expenses, conforming those costs to the expenses allowable for the Missouri county in which she lived. *See* Internal Revenue Manual (IRM) 5.15.1.10 (Nov. 17, 2014). In calculating expenses the SO did not allow mortgage expenses because petitioner supplied no proof that she lacked equity in the property. Subtracting her allowable monthly expenses from her revised monthly income, the SO informed petitioner that she still did not qualify for CNC status because she had the ability to pay $1,685 a month.

Because petitioner sought no collection alternative apart from CNC status and lien withdrawal, the SO decided to close the case. On August 19, 2020, the IRS issued petitioner a notice of determination sustaining the NFTL filing. The notice explained that petitioner could not challenge her underlying liability for the TFRPs because she had a prior opportunity, upon receiving the Letter 1153, to challenge those penalties at Appeals. The notice determined that petitioner did not meet the criteria for lien withdrawal under section 6323(j) and that, for the reasons discussed previously, CNC status was not available as a collection alternative.

Petitioner timely petitioned this Court, challenging her underlying liability for the TFRPs and the propriety of the collection action. Respondent filed a Motion for Summary Judgment, to which petitioner timely responded. She concedes receiving the Letter 1153 in 2015 but urges that she was undergoing stress at that time in connection with her divorce proceedings. She alleges that she "had no involvement with the business operations of Oasys . . . and did not sign any tax filings associated with the company." She challenges the tax lien placed on her home and the SO's calculation of her ability to pay, urging that the "monthly amount that was determined is unreasonable and not economically feasible."

Discussion

A. *Summary Judgment Standard*

Absent stipulation to the contrary, our decision in this case is appealable to the U.S. Court of Appeals for the Eighth Circuit. *See* § 7482(b)(1)(G). That court has held that, where de novo review is not applicable, the scope of review in a CDP case is confined to the administrative record. *See Robinette v. Commissioner*, 439 F.3d 455, 461 (8th Cir. 2006), *rev'g* 123 T.C. 85 (2004). Petitioner has supplied no reason to believe that the administrative record in this case is incomplete. Accordingly, in a case such as this, "summary judgment serves as a mechanism for deciding, as a matter of law, whether the agency action is supported by the administrative record and is not arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." *Belair v. Commissioner*, 157 T.C. 10, 17 (2021) (quoting *Van Bemmelen v. Commissioner*, 155 T.C. 64, 79 (2020)).

B. *Standard of Review*

Neither section 6320(c) nor section 6330(d)(1) prescribes the standard of review that this Court should apply in reviewing an IRS administrative determination in a CDP case. The general parameters for such review are marked out by our precedents. Where the validity of the taxpayer's underlying liability is properly at issue, we review the IRS's determination de novo. *Goza v. Commissioner*, 114 T.C. 176, 181–82 (2000). Where the taxpayer's underlying liability is not properly at issue, we review the IRS's decision for abuse of discretion only. *Id.* at 182. Abuse of discretion exists when a determination is arbitrary, capricious, or without sound basis in fact or law. *See Murphy v. Commissioner*, 125 T.C. 301, 320 (2005), *aff'd*, 469 F.3d 27 (1st Cir. 2006).

C. *Underlying Liability*

A taxpayer may challenge the existence or amount of her underlying tax liability in a CDP case only if she "did not receive any statutory notice of deficiency for such tax liability or did not otherwise have an opportunity to dispute" it. § 6330(c)(2)(B). TFRPs are "assessable penalties" and thus are not subject to deficiency procedures. *See Chadwick v. Commissioner*, 154 T.C. 84, 91 (2020). However, a taxpayer has the opportunity to dispute her liability for a TFRP by filing an appeal with the IRS when she receives a Letter 1153. *See Mason v. Commissioner*, 132 T.C. 301, 317–18 (2009); *Lewis v. Commissioner*, 128 T.C. 48, 61 (2007); *Thompson v. Commissioner*, T.C. Memo. 2012-87, 103 T.C.M. (CCH) 1470, 1472; Treas. Reg. § 301.6320-1(e)(3), Q&A-E2.

The IRS sent petitioner a Letter 1153 in July 2015. She acknowledges having received that letter, and the USPS Form 3811 bears her signature. The Letter 1153 informed petitioner of her right to appeal the proposed TFRP assessment and outlined the steps she needed to take. Because she had an opportunity to dispute her TFRP liability upon receipt of the Letter 1153 but declined to do so, she was not entitled to challenge her underlying tax liability at the CDP hearing and may not advance such a challenge in this Court. *See Chadwick*, 154 T.C. at 89. Accordingly, we review the SO's actions for abuse of discretion only.

D. *Abuse of Discretion*

In deciding whether the SO abused her discretion we consider whether she: (1) properly verified that the requirements of any applicable law or administrative procedure have been met; (2) considered any relevant issues petitioner raised; and (3) determined whether "any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of [petitioner] that any collection action be no more intrusive than necessary." § 6330(c)(3); *see* § 6320(c). Our review of the record establishes that the SO properly discharged all of her responsibilities under the statute.

1. *Innocent Spouse Relief*

During the CDP hearing petitioner urged that she was entitled to "innocent spouse" relief under section 6015. The SO advised petitioner that she was not eligible for such relief because her TFRP liabilities arose from Oasys's unpaid payroll taxes, not from a joint Federal income tax return. The SO made this determination after reviewing petitioner's Form 8857 and the correspondence from CCISO.[2]

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[2] Although petitioner is precluded from challenging her underlying liability, "[t]he limitations imposed under section 6330(c)(2)(B) do not apply to spousal defenses . . . [because] the taxpayer is not disputing the amount or existence of the liability itself, but asserting a defense to the liability." Treas. Reg. § 301.6320-1(e)(3), Q&A-E3. We need not decide whether the SO's resolution of petitioner's spousal defense challenge should be reviewed de novo rather than for abuse of discretion. We would decide this issue the same way under either standard because (as explained in the text) it presents a purely legal question.

Section 6015 is captioned “Relief from joint and several liability on joint return.” Section 6015(a)(1) provides that “an individual who has made a joint return may elect to seek relief under the procedures prescribed under subsection (b),” which sets forth procedures “applicable to all joint filers.” Section 6015(a)(2) provides that an individual may “elect to limit [her] liability for any deficiency with respect to such joint return in the manner prescribed under subsection (c),” which sets forth procedures applicable for spouses who are legally separated or no longer living together.

Subsections (b) and (c) both specify rules for obtaining relief from liabilities that are shown on (or should have been shown on) a joint Federal income tax return. *See* § 6015(b)(1)(A) and (B) (presupposing that “a joint return has been made” and that “on such return there is an understatement of tax”); § 6015(c)(1) (providing that a person “who has made a joint return” may be partially relieved of “liability for any deficiency which is assessed with respect to the return”).

Petitioner’s TFRP liabilities were not shown on, and did not arise from the filing of, a joint Federal income tax return. Rather, her TFRP liabilities arose from her failure to discharge her duty, as an officer of Oasys, to ensure that payroll taxes collected from the company’s workers were properly paid over to the Department of the Treasury. Petitioner was therefore not eligible for relief under section 6015(b) or (c).

Subsection (f) provides that “equitable relief” may be afforded to a taxpayer if “relief is not available to such individual under subsection (b) or (c).” § 6015(f)(1). “Under procedures prescribed by the Secretary,” such relief may be available if, “taking into account all the facts and circumstances, it is inequitable to hold the individual liable for any unpaid tax or any deficiency (or any portion of either).” *Ibid.* The SO determined that petitioner was likewise ineligible for relief under subsection (f).

The Commissioner has specified, in Rev. Proc. 2013-34, 2013-43 I.R.B. 397, the procedures governing equitable relief. These procedures confirm that subsection (f), like subsections (b) and (c), applies only to joint income tax liabilities. *See* Rev. Proc. 2013-34, § 1.01, 2013-43 I.R.B. at 397 (“This revenue procedure provides guidance for a taxpayer seeking equitable relief from income tax liability . . . .”). Indeed, the IRS will not consider a taxpayer's request for equitable relief unless she meets seven "threshold conditions," one of which is that the "income tax liability from which the requesting spouse seeks relief" is attributable to the non-requesting spouse. *Id.* § 4.01(7), 2013-43 I.R.B. at 399. Another condition is that "[t]he requesting spouse [must have] filed a joint return for the taxable year" for which relief is sought. *Id.* § 4.01(1).

The IRS assessed TFRPs against petitioner and her ex-husband upon determining that they were both responsible for Oasys's failure to remit payroll taxes to the Government. The IRS did not determine any income tax deficiencies against petitioner and has not attempted to collect any unpaid tax shown on any joint return that she signed. Although a TFRP liability is a form of "unpaid tax," section 6015(f) applies only to unpaid taxes or deficiencies arising from joint income tax returns. *See* Treas. Reg. § 1.6015-1(a)(1)(iii) (stating that section 6015(f) applies only to "joint and several liability for Federal income tax"); H.R. Rep. No. 105-599, at 254 (1998) (Conf. Rep.), *reprinted in* 1998-3 C.B. 747, 1008 (stating that section 6015(f) applies only to "any unpaid tax or deficiency arising from a joint return"). The SO therefore did not err when she advised petitioner that innocent spouse relief was not available to her.

2. *Collection Alternatives*

Having rejected petitioner's underlying liability and spousal defense challenges, the SO proceeded to consider collection alternatives. The principal issue petitioner raised was her entitlement to have her account placed in CNC status. To be entitled to this collection alternative taxpayers must demonstrate that, on the basis of their assets, equity, income, and expenses, they have no apparent ability to make payments on the outstanding tax liability. *See Foley v. Commissioner*, T.C. Memo. 2007-242, 94 T.C.M. (CCH) 210, 212; IRM 5.16.1.1 (Sept. 18, 2018).

A taxpayer's ability to make payments is determined by calculating the excess of income over necessary living expenses. *Rosendale v. Commissioner*, T.C. Memo. 2018-99, 116 T.C.M. (CCH) 4, 6; IRM 5.16.1.2.9 (Sept. 18, 2018). An SO does not abuse her discretion when she employs local and national standards to calculate the taxpayer's expenses and ability to pay. *See Friedman v. Commissioner*, T.C. Memo. 2013-44, 105 T.C.M. (CCH) 1288, 1290 (noting that burden is on taxpayer to justify departure from local standards). In reviewing for abuse of discretion, the Court does not substitute its judgment for that of the SO or recalculate a taxpayer's ability to pay. *See Norberg v. Commissioner*, T.C. Memo. 2022-30, at *5; *O'Donnell v. Commissioner*, T.C. Memo. 2013-247, 106 T.C.M. (CCH) 477, 481.

The collection specialist to whom the SO initially referred petitioner's request concluded that she did not qualify for CNC status because she could pay $2,831 per month toward her TFRP liability. The SO agreed that petitioner's income should be adjusted downward and recalculated her ability to pay as $1,685 per month. In determining this figure, the SO calculated allowable monthly expenses by reference to local standards prevailing in the Missouri county where petitioner resided. This caused a downward adjustment to certain expenses that petitioner reported on her Form 433–A.

Petitioner contends that "the calculated monthly amount that was determined was unreasonable and not economically feasible." This contention is based in part on the expenses petitioner claimed on her Form 433–A, without reference to prevailing local standards. The SO was authorized to rely on those standards in assessing petitioner's ability to pay, and it was her burden to justify a departure from the local standards. *Friedman*, 105 T.C.M. (CCH) at 1290. Petitioner has not satisfied that burden.

Petitioner challenges two aspects of the SO's calculation apart from the use of prevailing local expense standards. First, she urges that the SO should have included home mortgage expenses of $1,611 per month. The SO did not allow this expense because petitioner supplied no proof "that there was no equity in the home." *See* IRM 5.16.1.2.9(1) ("An account should not be reported as CNC if the taxpayer has income or equity in assets, and enforced collection of the income or assets would not cause hardship.").

In her response to the summary judgment motion, petitioner says that she "do[es] not have access" to any equity in the property. Although the meaning of this statement is not entirely clear, we find it beside the point. Petitioner does not dispute that she neglected to provide any evidence to the SO regarding her possession of equity in the property. The SO was obligated to make a decision based on the evidence that petitioner submitted during the CDP hearing. The SO did not abuse her discretion by neglecting to consider evidence petitioner did not submit.

Petitioner also alleges that the monthly child support she receives from her ex-husband was recently reduced, as of July 2021, from $1,400 to $1,000 per month. Again, this information was not available to the SO when she made her decision in August 2020. In any event a $400 reduction in her monthly income would not have altered the SO's determination that petitioner was not entitled to CNC status.

The other collection alternative petitioner proposed was withdrawal of the NFTL. Section 6323(j)(1) authorizes that relief if (1) "the filing of such notice was premature or otherwise not in accordance with administrative procedures," (2) the taxpayer has entered into an installment agreement that renders the NFTL unnecessary, (3) withdrawal of the NFTL "will facilitate the collection of the tax liability," or (4) withdrawal of the NFTL "would be in the best interests of the taxpayer (as determined by the National Taxpayer Advocate) and the United States."

The notice of determination correctly concluded that petitioner had failed to establish the existence of any of these conditions. The second and fourth factors are inapplicable here. Petitioner did not contend that the NFTL filing was premature or improper. And she offered no evidence that withdrawal of the NFTL would facilitate collection of the TFRP liability.

The only collection alternatives petitioner proposed, in her CDP hearing request or subsequently, were to have her account placed in CNC status and to have the NFTL withdrawn. The SO did not abuse her discretion in denying those forms of relief. In her response to the summary judgment motion petitioner suggests that she might be able to make some payment toward her tax liability, albeit in a monthly amount smaller than the SO calculated. If so, petitioner is free to submit to the IRS at any time, for its consideration and possible acceptance, a collection alternative in the form of an installment agreement or an offer-in-compromise, supported by up-to-date financial information (including any relevant information about equity in her home and reduced child support payments).

To implement the foregoing,

An appropriate order and decision will be entered for respondent.

MICHAEL D. BROWN, PETITIONER *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket No. 11519-20L. Filed June 23, 2022.

P has a tax liability that exceeds $50 million. In an effort to collect a portion of this unpaid liability, R issued P a Letter 3172, Notice of Federal Tax Lien Filing and Your Right to a Hearing. P timely requested a collection due process (CDP) hearing. In April 2018, at the outset of the CDP hearing, P submitted an offer-in-compromise (OIC). R processed the OIC and forwarded it to a collection specialist for review. In November 2018 the collection specialist informed P that his file had been closed and that the offer was being returned to him because "[o]ther investigations are pending that may affect the liability sought to be compromised or the grounds upon which it was submitted." During the CDP hearing P urged R to overturn that decision. R concluded that the OIC was correctly returned to P and proceeded to close the CDP case. In August 2020 R issued a notice of determination, and P timely petitioned this Court. P has filed a Motion for Summary Judgment contending that his OIC was "deemed accepted" by R under I.R.C. § 7122(f). That section provides that an OIC is "deemed to be accepted" if it "is not rejected by the Secretary before the date which is 24 months after the date of the submission of such offer." P argues that the rejection occurred 27 months after his OIC was submitted, i.e., in August 2020, when R issued the notice of determination. R contends that the rejection occurred 7 months after the OIC was submitted, i.e., in November 2018, when the collection specialist returned the OIC to P and closed the file on his offer. *Held*: P's OIC was "rejected by the Secretary" in November 2018, when the collection specialist closed the file and returned the OIC to P. Because P's OIC was "rejected by the Secretary" within 24 months of submission, it was not deemed accepted under I.R.C. § 7122(f). *Held, further*, the time during which the IRS Appeals Office in a CDP case reviews the return of an OIC

is not included as part of the 24-month "deemed acceptance" period of I.R.C. § 7122(f). *See* Treas. Reg. § 301.7122-1(d)(2); Notice 2006-68, § 1.07, 2006-2 C.B. 105, 106.

Steven Ray Mather, for petitioner.
Kevin W. Coy and *Jeremy J. Eggerth*, for respondent.

OPINION

LAUBER, *Judge*: In this collection due process (CDP) case, petitioner seeks review of a determination by the Internal Revenue Service (IRS or respondent) to reject an offer-in-compromise (OIC). After the settlement officer (SO) assigned to petitioner's case received the OIC, it was referred to a collection specialist for evaluation. Six months later, the collection specialist returned the OIC to petitioner and closed the file on his offer. Petitioner sought review of that decision during the CDP hearing, but the SO determined that the OIC had correctly been returned because it was no longer processable. The IRS then issued petitioner, on August 12, 2020, a notice of determination sustaining the collection action.

Petitioner has filed a Motion for Summary Judgment contending that his OIC is deemed to have been accepted under section 7122(f).[1] That statute provides that an OIC "shall be deemed to be accepted" if it "is not rejected by the Secretary before the date which is 24 months after the date of the submission of such offer." § 7122(f). Petitioner argues that the rejection occurred 27 months after the OIC was submitted, i.e., in August 2020, when the IRS issued the notice of determination closing the CDP case. Respondent contends that the rejection occurred 7 months after the OIC was submitted, i.e., in November 2018, when the IRS returned the OIC to petitioner. Agreeing with respondent on that point, we conclude that the IRS rejected petitioner's OIC within the 24-month period specified in section 7122(f), so that his offer was not "deemed accepted." We will therefore deny petitioner's Motion.

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[1] Unless otherwise indicated, all statutory references are to the Internal Revenue Code (Code), Title 26 U.S.C., in effect at all relevant times, all regulation references are to the Code of Federal Regulations, Title 26 (Treas. Reg.), in effect at all relevant times, and all Rule references are to the Tax Court Rules of Practice and Procedure.

Background

The following facts are derived from the pleadings, the parties' motion papers, and the exhibits and declarations attached thereto. They are stated solely for the purpose of ruling on petitioner's Motion and not as findings of fact in this case. *See Sundstrand Corp. v. Commissioner*, 98 T.C. 518, 520 (1992), *aff'd*, 17 F.3d 965 (7th Cir. 1994). Petitioner resided in California when he petitioned this Court.

This is the third CDP case petitioner has prosecuted in this Court. *See Brown v. Commissioner* (*Brown IV*), T.C. Memo. 2021-112, *supplementing Brown v. Commissioner* (*Brown II*), T.C. Memo. 2019-121, *aff'd in part, vacated in part, and remanded*, *Brown v. Commissioner* (*Brown III*), 826 F. App'x 673 (9th Cir. 2020); *Brown v. Commissioner* (*Brown I*), T.C. Memo. 2016-82, *aff'd*, 697 F. App'x 1 (D.C. Cir. 2017). At issue in the previous cases were collection actions relating to petitioner's 2001–2007 and 2014 tax years. This case concerns collection action for petitioner's 2009 and 2010 tax years. Petitioner's total outstanding liability for all years exceeds $50 million. *See Brown II*, 118 T.C.M. (CCH) 260, 261.

On November 9, 2017, in an effort to collect the balance due for 2009 and 2010, the IRS issued petitioner Letter 3172, Notice of Federal Tax Lien Filing and Your Right to a Hearing. Petitioner timely requested a CDP hearing, checking the box "Offer in Compromise." On April 19, 2018, he submitted Form 656, Offer in Compromise, in which he offered to pay $320,000 in satisfaction of his liabilities for 2009–2010 (and other years).

This was not the first OIC petitioner had submitted to the IRS. In November 2016 he submitted an OIC in which he offered to pay $400,000 in satisfaction of his total outstanding liabilities for all years. *See Brown II*, 118 T.C.M. (CCH) at 261. He submitted that OIC during a CDP hearing, and the SO assigned to the case referred it to the IRS's Centralized Offer in Compromise Unit (COIC unit). *Id.* at 262. In April 2017 the COIC unit returned the offer to petitioner, concluding that it was no longer processable because there was an ongoing IRS investigation of an "abusive tax avoidance transaction" involving petitioner. *Ibid.* The SO thereafter issued a notice of determination, concluding that petitioner's OIC had correctly been returned "because there were other investigations pending . . . that might affect [his] delinquent tax account sought to be compromised." *Ibid.*

In *Brown II* petitioner argued (among other things) that the IRS had not formally "rejected" his OIC within the meaning of section 7122(f). Without a formal rejection, he asserted, the OIC should be deemed to have been accepted under section 7122(f). We found no merit in that argument, holding that the COIC unit "correctly returned petitioner's OIC on April 6, 2017, at which point his OIC was considered closed." *Id.* at 264. We explained that "the 24-month statutory period of automatic acceptance prescribed in section 7122(f) ends when the COIC unit returns a taxpayer's OIC." *Id.* at 263 (citing Internal Revenue Manual (IRM) 8.23.3.1.1.1(6) (Oct. 15, 2014)). Because the COIC unit returned petitioner's offer within the 24-month period, his offer was not "deemed accepted." *Id.* at 264.

In October 2020 the U.S. Court of Appeals for the Ninth Circuit affirmed this part of our decision. The Ninth Circuit ruled that, under section 7122(f), an OIC "will not be deemed to be accepted if the offer is, within the 24-month period, rejected by the [IRS], [or] returned by the [IRS] to the taxpayer as nonprocessable or no longer processable." *Brown III*, 826 F. App'x at 674 (quoting Notice 2006-68, § 1.07, 2006-2 C.B. 105, 106). Petitioner's OIC was "returned" within the 24-month period; the Ninth Circuit accordingly affirmed our conclusion that his offer was not "deemed accepted." *Ibid.*

While litigating these other CDP cases, petitioner submitted the (substantially similar) OIC at issue here. The instant case was assigned to SO James Feist in the IRS Independent Office of Appeals (Appeals) in Tampa, Florida. On March 8, 2018, SO Feist scheduled a telephone conference with petitioner's counsel, which was held on April 12, 2018. Petitioner's counsel indicated that he would be submitting an OIC, which he sent to SO Feist a week later. SO Feist forwarded the offer to the COIC unit, which determined in May 2018 that the offer appeared to be "processable," i.e., that it met IRS formal requirements. Petitioner's offer was then referred to a collection specialist in the IRS's Laguna Niguel branch (Laguna Group).

On November 5, 2018, the Laguna Group issued petitioner a letter informing him that the IRS had "closed [the] file" and was “returning your Form 656, Offer in Compromise” because “[o]ther investigations are pending that may affect the liability sought to be compromised or the grounds upon which it was submitted.” The Laguna Group explained: “As of the date of this letter, we are considering your offer closed. Any payments received with your offer or after the date of this letter will be applied to your liability.” Attached to the letter was a copy of petitioner’s original offer packet, marked “RETURNED.”

For roughly a year and a half after receiving that letter, petitioner took the position in the CDP hearing that the Laguna Group had erred in returning his offer. On November 15, 2018, his counsel told SO Feist that the reason given by the collection specialist for rejecting the offer—the pendency of other investigations—was “bogus.” On February 22, 2019, petitioner’s counsel called SO Feist and requested reconsideration of the Laguna Group’s decision. SO Feist replied that “Appeals will maintain jurisdiction of [the] case,” but advised that it would be “difficult[] [to] overturn[] the reasons [given by the collection specialist] for the return of [the] OIC.” The CDP case then remained open during the pendency of the “other investigations” to which the collection specialist had referred.

On June 23, 2020—more than 24 months after the offer was submitted—petitioner’s counsel advanced a new argument in a letter to SO Feist. Petitioner now urged that “only Appeals can make the determination to return the OIC.” Because “Appeals did not return the OIC” within 24 months of the offer’s submission, petitioner insisted that the OIC was “deemed accepted” under section 7122(f).

Upon reviewing the letter, SO Feist called petitioner’s counsel and expressed agreement with the Laguna Group’s decision to return the OIC. SO Feist indicated that he intended to close the CDP case unless petitioner wished to propose a different collection alternative. Petitioner did not propose a different collection alternative, and SO Feist proceeded to close the case.

On August 12, 2020, the IRS issued petitioner the notice of determination on which this case is based. The notice of determination concluded that petitioner’s OIC was correctly returned by the Laguna Group because of an ongoing IRS investigation. The notice states that, as a result of this investigation, the IRS in February 2019 referred petitioner's information to the U.S. Department of Justice "to reduce the Federal tax debts to judgment."[2]

Petitioner timely petitioned this Court. On July 22, 2021, he filed the instant Motion, contending that the OIC was deemed accepted under section 7122(f). Respondent timely objected to the Motion, and we heard oral argument on March 28, 2022. Further briefing ensued.

Discussion

A. *Summary Judgment Standard*

The purpose of summary judgment is to expedite litigation and avoid costly, unnecessary, and time-consuming trials. *See FPL Grp., Inc. & Subs. v. Commissioner*, 116 T.C. 73, 74 (2001). We may grant summary judgment regarding an issue as to which there is no genuine dispute of material fact and a decision may be rendered as a matter of law. Rule 121(b); *Sundstrand Corp.*, 98 T.C. at 520. The sole question presented at this stage of the proceedings is whether petitioner's OIC was deemed accepted under section 7122(f). This question is principally one of law, and no material facts are in genuine dispute. We conclude that this issue may be adjudicated summarily.

B. *Analysis*

Section 7122(f) is captioned, "Deemed acceptance of offer not rejected within certain period." It provides: "Any offer-in-compromise submitted under this section shall be deemed to be accepted by the Secretary if such offer is not rejected by the Secretary before the date which is 24 months after the date of the submission of such offer." § 7122(f). We must decide

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[2] Because the IRS has allegedly referred petitioner's information to the Department of Justice "to reduce the Federal tax debts to judgment," respondent advances the alternative contention that, as of February 2019, the Commissioner was no longer authorized to consider petitioner's OIC. *See* § 7122(a) ("The Secretary may compromise any civil or criminal case . . . *prior to* reference to the Department of Justice for prosecution or defense . . . ." (Emphasis added.)). Given our disposition, we need not address respondent's alternative argument at this stage of the case.

whether petitioner's OIC was "rejected by the Secretary" in November 2018, when the Laguna Group returned the OIC to him, or in August 2020, when Appeals issued the notice of determination sustaining the Laguna Group's decision.

The Secretary has promulgated regulations addressing the compromise of tax liabilities under section 7122. The regulations provide that "[a]n offer to compromise becomes pending when it is accepted for processing." Treas. Reg. § 301.7122-1(d)(2). If the IRS accepts an offer for processing but subsequently determines that it was (or has become) nonprocessable, or that the offer is nonreviewable for other reasons, the offer may be returned to the taxpayer. *Ibid.* "An offer returned following acceptance for processing is deemed pending only for the period between the date the offer is accepted for processing and the date the IRS returns the offer to the taxpayer." *Ibid.*

The regulations provide that a taxpayer must submit an OIC "according to the procedures, and in the form and manner, prescribed by the Secretary." *Id.* para. (d)(1). The Secretary has prescribed the relevant procedures in Rev. Proc. 2003-71, 2003-2 C.B. 517, and in Notice 2006-68, 2006-2 C.B. 105, which explains the "deemed acceptance" rules of section 7122(f). The Notice states that "[a]n offer will not be deemed to be accepted if the offer is, within the 24-month period, rejected by the Service [or] returned by the Service as nonprocessable or no longer processable." § 1.07, 2006-2 C.B. at 106. If a taxpayer requests review of a rejection, "[t]he period during which the IRS Office of Appeals considers a rejected offer in compromise is not included as part of the 24-month period." *Ibid.*

Petitioner submitted his OIC to SO Feist, the Appeals officer handling the CDP case. In May 2018 SO Feist sent the offer to the COIC unit, which concluded that the offer appeared to be processable. The COIC unit then referred the offer to a collection specialist in the Laguna Group. Six months later, on November 5, 2018, the Laguna Group determined that the OIC was no longer processable because of an ongoing investigation "that may affect the liability sought to be compromised." The Laguna Group accordingly returned the offer to petitioner and informed him that it had closed its file on his offer. Enclosed with that letter was a physical copy of petitioner's OIC, marked "RETURNED."

For purposes of section 7122(f), petitioner's OIC was "deemed pending only for the period between the date the offer [wa]s accepted for processing and the date the IRS return[ed] the offer to [him]." Treas. Reg. § 301.7122-1(d)(2). His offer was accepted for processing in May 2018, but it was returned six months later in November 2018. *See* Rev. Proc. 2003-71, § 5.06, 2003-2 C.B. at 518 ("An offer to compromise is considered to be returned on the day the Service mails, or personally delivers, a written letter to the taxpayer informing the taxpayer of the decision to return the offer."). Because the IRS returned petitioner's OIC within 24 months of submission, his OIC was not deemed accepted under section 7122(f).

The outcome is the same under the regulatory provisions governing rejections outside the CDP context. A rejection of an OIC ordinarily includes a "written notice" explaining the decision and providing the right to seek review in Appeals. *See* Treas. Reg. § 301.7122-1(f)(1). But it is the initial rejection, not the final determination by Appeals, that is relevant for purposes of section 7122(f). The initial rejection terminates the 24-month period "because the offer was rejected by the Service within the meaning of section 7122(f) prior to consideration of the offer by the Office of Appeals." Notice 2006-68, § 1.07, 2006-2 C.B. at 106. In other words, "[t]he period during which the IRS Office of Appeals considers a rejected offer in compromise is not included as part of the 24-month period." *Ibid.*

After receiving the Laguna Group's decision, petitioner asserted that the basis for its decision was "bogus" and should be overturned by SO Feist. But the time SO Feist spent evaluating petitioner's position is not taken into account under section 7122(f). The OIC had already been returned (i.e., "rejected by the Secretary" or his delegate), and the period during which Appeals conducted its review "is not included as part of the 24-month period." *See* §§ 7122(f), 7701(a)(11)(B), (12)(A); Notice 2006-68, § 1.07, 2006-2 C.B. at 106.

Petitioner acknowledges that, under Treasury Regulation § 301.7122-1 and Notice 2006-68, the 24-month period would ordinarily have terminated in November 2018, when the Laguna Group returned the OIC to him. He does not challenge the validity of these authorities; rather, he asserts that they are inapplicable to "CDP OICs." When an OIC is submitted in a CDP case, petitioner says, "only an Appeals notice of determination can be the event that terminates" the 24-month period.

Petitioner floated a similar theory in *Brown II* and *Brown III*, but this Court and the Ninth Circuit both demurred to his argument. In that case (as in this) petitioner submitted his OIC to the SO who conducted the CDP hearing. *See Brown II*, 118 T.C.M. (CCH) at 261–62. The SO forwarded the offer to the COIC unit, which promptly returned the offer to petitioner because an ongoing IRS investigation "might affect [the] delinquent tax account sought to be compromised." *Id.* at 262. Petitioner urged that this action did not amount to a "rejection" within the meaning of section 7122(f), so that his OIC was "deemed accepted."

We dismissed that argument in *Brown II*, ruling that "the 24-month statutory period of automatic acceptance prescribed in section 7122(f) ends when the COIC unit returns a taxpayer's OIC." *Id.* at 263 (citing IRM 8.23.3.1.1.1(6)). Petitioner appealed, but the Ninth Circuit in *Brown III* affirmed that portion of our decision. It ruled that "an offer 'will not be deemed to be accepted if the offer is, within the 24-month period, rejected by the [IRS], [or] returned by the [IRS].'" *Brown III*, 826 F. App'x at 674 (quoting Notice 2006-68, § 1.07, 2006-2 C.B. at 106). That is precisely what happened, again, in the instant case.

Petitioner seeks to distinguish *Brown II* and *Brown III* on the theory that the COIC unit's return letter and the SO's notice of determination were both issued there within a span of two years. We do not see how this distinction helps petitioner. This Court unambiguously ruled in *Brown II* that the statutory 24-month period "ends when the COIC unit returns a taxpayer's OIC." *Brown II*, 118 T.C.M. (CCH) at 263. The Ninth Circuit likewise ruled that an offer is not deemed accepted if it is "returned by the [IRS]" within the 24-month period. *Brown III*, 826 F. App'x at 674. Both courts clearly identified the terminating event as the COIC unit's return of the offer, not the SO's notice of determination. Indeed, neither court could possibly have been referring to the notice of determination: In that notice the SO did not return the OIC, but rather sustained the correctness of the COIC unit's prior action in returning the OIC.

Petitioner invites us to reconsider our holding in *Brown II*, asserting that the Laguna Group's decision to return the OIC was "procedurally meaningless" and that "CDP OICs" are governed exclusively by section 6330(c), which requires a final determination by Appeals. We decline to reconsider our holding in *Brown II*, and we are not at liberty to "reconsider" the Ninth Circuit's ruling in *Brown III*. Precedent apart, petitioner's argument is meritless because it confuses two kinds of finality: the administrative return of an OIC, which terminates the 24-month period under section 7122(f), and the notice of determination, which terminates the CDP proceeding under section 6330.

Under section 6330(c) a taxpayer in a CDP case may raise numerous issues, including underlying liability challenges, spousal defenses, the propriety of the collection action, and the availability of collection alternatives. *See* § 6330(c)(2). The SO must consider all issues raised by the taxpayer, and his ultimate decision on each point makes up the "determination." *See* § 6330(c)(3). That "determination" can then be reviewed in this Court. *See* § 6330(d)(1).

The Laguna Group's November 2018 letter returning petitioner's offer was a "rejection" for purposes of section 7122(f). As we ruled in *Brown II* and as the Ninth Circuit ruled in *Brown III*, the return of an OIC that is no longer processable is a form of rejection, albeit based on procedural grounds rather than substantive evaluation of the offer's merits. But the Laguna Group's decision to return the OIC was not final: It was up to SO Feist to decide whether the Laguna Group had acted properly. During the CDP hearing petitioner was free to submit facts and argument urging that the Laguna Group had erred in returning the offer. Petitioner did so by contending that the ground the Laguna Group had relied on—the pendency of other IRS investigations—was "bogus."

SO Feist evaluated petitioner's argument, found it meritless, and sustained the Laguna Group's decision to return the OIC. Under section 6330(d) we have jurisdiction to review SO Feist's ultimate conclusions as embodied in the notice of determination, not the Laguna Group's initial decision to return the offer. But the fact that the Laguna Group's decision was not "final" for purposes of judicial review does not prevent it from being a "return" or a "rejection" under section 7122(f), for the limited purpose of terminating the 24-month "deemed acceptance" period.[3]

In essence petitioner contends that section 6330 overrides sub silentio the outcome dictated by section 7122(f), asserting that the notice of determination is the "critical event" under section 7122(f) and that "there is no real authority that suggests a contrary result." This assertion ignores Treasury Regulation § 301.7122-1, *Brown II*, *Brown III*, Notice 2006-68, and the IRM provisions discussed previously. These authorities confirm that the IRS's initial decision to return an OIC is the event that terminates the 24-month "deemed acceptance" period. Petitioner has cited no authority for the proposition that section 7122(f) has a different meaning when the offer is made in a CDP context.

Our conclusion is fully consistent with the statute's purpose. Section 7122(f) was added to the Code as part of the Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA), Pub. L. No. 109-222, § 509(b)(2), 120 Stat. 345, 363 (2006). In enacting section 7122(f) Congress expressed its expectation that the IRS would respond fairly promptly to OICs, rather than letting them sit in a pile for two years or more. *See* H.R. Rep. No. 109-455, at 234 (2006) (Conf. Rep.), *reprinted in* 2006 U.S.C.C.A.N. 234, 421. Here the IRS was faithful to Congress' mandate: It took prompt action on petitioner's OIC, returning

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[3] Petitioner errs in relying on a section of the IRM captioned "TIPRA Statute Responsibilities." *See* IRM 8.22.7.10.1.3 (Sept. 23, 2014). As in effect when petitioner submitted his offer, this section instructed SOs that an OIC would be deemed accepted only if it was "not rejected, returned or withdrawn within 24 months of submission." *Id.* 8.22.7.10.1.3(1). Petitioner does not dispute that his OIC was "returned" within 24 months of submission. That IRM section currently provides that "[c]ertain dispositions made by Collection during consideration of a CDP OIC will result in the closing of the TIPRA 24-month period." IRM 8.22.7.10.1.3(5) (Aug. 26, 2020). These dispositions include the return of the offer, the mandatory withdrawal of an offer, and an erroneously issued rejection letter. The IRM says that these dispositions "will close the TIPRA 24-month period even if determined by Appeals to have been erroneously made." *Ibid.* This current IRM provision is likewise consistent with Notice 2006-68, § 1.07, 2006-2 C.B. at 106, which states that "[t]he period during which the IRS Office of Appeals considers a rejected offer in compromise is not included as part of the 24-month period."

the offer to him within six months and explaining why his offer was no longer processable.

Because petitioner's OIC was submitted in connection with a CDP proceeding, he had the opportunity to ask SO Feist to review the Laguna Group's decision.[4] And SO Feist did not complete his review of the entire case within 24 months. But there is no reason to believe that Congress, in enacting section 7122(f), intended to place a limit on the duration of the CDP proceeding, i.e., on the length of time a taxpayer can negotiate with Appeals before a notice of determination is issued. *See* Treas. Reg. § 301.6320-1(e)(3)(ii), Q&A E-9 (noting that Appeals has no deadline to issue a notice of determination).

It is not uncommon for taxpayers to submit an OIC (as petitioner did here) at the outset of a CDP hearing. If that offer is returned by the COIC unit, the taxpayer may urge the SO to reverse that decision, but the taxpayer may also pursue other options. He might challenge his underlying liability, request "innocent spouse" relief, propose an installment agreement, or seek withdrawal of a tax lien filing. These issues may require the SO to evaluate multiple submissions of financial information, seek assistance from the IRS Examination Division, and/or consult with the IRS's Cincinnati Centralized Innocent Spouse Operation. Even absent a pandemic, these events may consume a considerable amount of time and possibly prolong the CDP case beyond 24 months. The Secretary recognized this possibility in Notice 2006-68, § 1.07, 2006-2 C.B. at 106, directing that "[t]he period during which the IRS Office of Appeals considers a rejected offer in compromise is not included as part of the 24-month period."

Acceptance of petitioner's argument—that Appeals must issue the notice of determination within 24 months after an OIC is submitted—could place the SO in a dilemma. If the SO by that deadline has not resolved every issue raised by the taxpayer, the SO could be motivated to issue a notice of

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[4] Outside the CDP context, if the IRS returns an OIC as nonprocessable, the taxpayer is not entitled to Appeals review of that action. *See* Treas. Reg. § 301.7122-1(f)(5)(ii). But the taxpayer *is* entitled to Appeals review if his OIC is returned during a CDP hearing. *See Mason v. Commissioner*, T.C. Memo. 2021-64, 121 T.C.M. (CCH) 1485, 1490 (noting that, in CDP cases, "we can review a determination to reject an OIC on grounds that would have triggered a *return* if the OIC had been submitted outside the CDP hearing process").

determination prematurely, lest the OIC be "deemed accepted." But doing so would risk reversal and remand for failure to address all "relevant issue[s] relating to the unpaid tax or the proposed [collection action]." § 6330(c)(2)(A). That would prolong the case even further, defying logic and undermining Congress' intent.[5]

For all these reasons, we hold that the OIC petitioner submitted in May 2018 was not "deemed accepted" under section 7122(f). Petitioner's arguments to the contrary are at odds with judicial precedent and derive no support from legal authority, policy considerations, or common sense. His Motion for Summary Judgment will therefore be denied.

To reflect the foregoing,

An appropriate order will be issued.

[5] Acceptance of petitioner's theory could also invite gamesmanship and abuse. An improperly motivated taxpayer could submit an OIC at the outset of a CDP case and then engage in delay tactics in an effort to extend the proceeding to a date beyond the 24th month. It is obvious that Congress did not wish to encourage this type of behavior. *Cf.* § 7122(g) (authorizing the IRS to ignore "frivolous submissions").